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Economist Conferences
Fourth China Branding Roundtable
Winning moves for a changing game
September 18th-19th 2007 Beijing

Print Edition June 16th 2001

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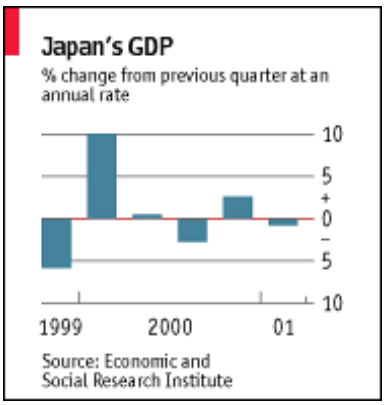
Business this week

Jun 14th 2001
From The Economist print edition

Contractions

Yet another recession seems to be hitting **Japan**. GDP contracted by 0.8% in the first quarter compared with the previous quarter at an annual rate. The current-account surplus shrank in April by 24% compared with a year earlier, as the slowdown of the world economy affected Japan's exports. The yen slid more against both the dollar and euro.



Britain's European partners imposed on it a European directive on **workers' rights** that requires companies to consult staff about job cuts and other restructuring. Employers moaned. The pound fell against the euro as entry to the single currency looked increasingly likely, but not at the pound's current high rate.

See article: EU workers' rights

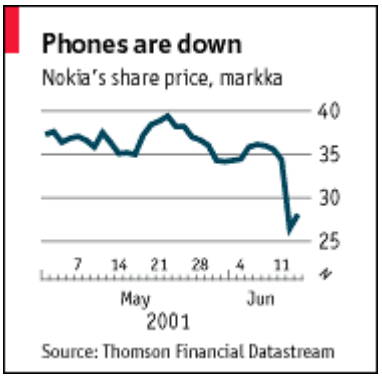
Inflation in **Europe** gave cause for concern. British and French inflation, both at 1.8% in April, increased to 2.1% and 2.3% respectively in May. Spain's inflation hit 4.2% from 4.0%. Luxembourg, Greece and Norway all recorded faster price rises as well.

Zimbabwe's government raised the price of fuel by nearly 70%, deepening an economic crisis. The country's main trade union said that over three-quarters of Zimbabweans already live below the poverty line.

After President Thabo Mbeki intervened, **South Africa**'s government struck a deal with the mining industry over new legislation designed to increase involvement by black entrepreneurs.

Calling charges

Nokia, the world's biggest maker of mobile phones, saw its share price plunge after revealing that sales growth would be lower than forecast and that second-quarter profits would suffer. Nokia insists, however, that sales will improve as new technology is introduced.



See article: The mobile-phone industry at a turning point

Standard & Poor's downgraded the debt of **Lucent Technologies**, a struggling telecoms-equipment maker, to junk status. Higher borrowing costs will not help the firm. Nor will contracting demand for telecoms equipment.

The board of **Eircom**, Ireland's former monopoly telecoms operator, is to recommend a *euro*2.9 billion ($2.5 billion) bid from Valentia, a consortium headed by Tony O'Reilly, an Irish media tycoon.

The chief executive of **Sonera**, a partly privatised Finnish telecoms operator, resigned, hinting that government interference was to blame. The firm, heavily indebted after investing in third-generation mobile licences, is now leaderless while rumours abound of a takeover by Sweden's Telia.

British Telecom and **Deutsche Telekom** agreed to share the building of third-generation mobile networks in Britain and Germany. The companies could save up to *euro*4 billion ($3.4 billion) between

them. BT raised £2.3 billion ($3.2 billion) from the sale of property in Britain.

Axa questions

Claude Bébéar, chairman of the supervisory board of **Axa**, a huge French insurance company, and Henri de Castries, its chief executive, were questioned by police investigating money-laundering at PanEuroLife, a Luxembourg company owned by Axa in 1996-98. PanEuroLife is suspected of complicity in helping French citizens to evade taxes.

See article: French investigations into money-laundering

Accenture, formerly Andersen Consulting, a management consultancy, announced details of an initial public offering that would value the firm at up to $15 billion. Accenture's 2,500 partners will be offered 80% of the shares. Less lucky: 600 staff whom Accenture intend to lay off and 800 more facing up to a year off on 20% pay.

Philip Morris sold 16% of **Kraft**, an American food giant, in an initial public offering valuing the company at $53.8 billion. America's second-largest IPO will raise around $8.7 billion, which Philip Morris will use to pay off debt.

The European Commission began investigating whether **Electricité de France**, an acquisitive French power company, had received any illegal state aid. Italy and Spain responded to EDF's predatory moves on domestic power companies with emergency laws meant to fend off the French firm.

A link-up scheme between state-owned Caisse des Dépôts et Consignations and the mutually owned Caisse d'Epargne will create France's **third-biggest banking group** by assets.

Strike aircraft

Lufthansa, Germany's flag-carrying airline, cut its forecast for operating profit in 2001 by about a third to as little as *euro*700m ($596m), blaming a *euro*125m pay deal with pilots and the cost of several strikes on top of a faltering world economy. Pilots at other airlines have observed the wage rise with interest.

EPA

General Electric offered the European Commission more concessions to secure approval of its planned $40 billion merger with **Honeywell**. GE said it would sell bits of Honeywell's aerospace business as well as its regional jet-engine and marine-engine divisions. Negotiations with the commission continued in a fraught atmosphere as the deadline loomed.

Months after abandoning a merger because of regulatory difficulties, **British Airways** and **KLM Royal Dutch** started talks aimed at "alternative forms of co-operation". BA and its partner, American Airlines, also met America's transport secretary to ask for antitrust immunity to allow a deepening of their alliance.

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Politics this week

Jun 14th 2001
From The Economist print edition

Bush's grand tour

EPA

George Bush arrived in Europe. First stop, Spain, on his way to NATO's headquarters in Belgium, then to Gothenburg in Sweden to meet summiteering EU leaders, and on to Poland and Slovenia. Big issues: missile defence ("We'll do it our way") and global warming (more research needed, no resuscitation of Kyoto). Vladimir Putin, Russia's president,will later meet Mr Bush in Slovenia.

See article: George Bush's European tour

Ariel Sharon, with seeming reluctance, and Yasser Arafat, with real reluctance, accepted a **Middle East** ceasefire brokered by George Tenet, the CIA's director. Israel said it would start to pull back its troops if the ceasefire held. But Mr Arafat has to sell it to a deeply suspicious Palestinian people.

See article: A precarious Israeli-Palestinian ceasefire

Timothy McVeigh was executed in Terre Haute, Indiana. The Oklahoma City bomber went to his death without any real apology to his victims.

See article: The end for McVeigh

Europe's bigger problem

Enlargement of the EU goes ahead anyway, claimed the European Commission, after **Ireland**'s voters rejected the Nice treaty, by 54% to 46%. I'll ask them again, said Ireland's prime minister, Bertie Ahern, wiping omelette off his face.

See article: The EU's Irish headache

Masochists queued up to lead **Britain**'s Conservative Party, after yet another general- election trouncing and the resignation of its leader, William Hague. Tony Blair reshaped his cabinet. Out as foreign secretary went Robin Cook, to be replaced by Jack Straw, hitherto home secretary. Women now hold seven (of 23) cabinet seats.

See article: Blair shuffles the pack

Bulgarians prepared to elect a new parliament on June 17th. Likely winner: their ex-King Simeon's party.

See article: Ex-King Simeon II looks likely to win power

In **Germany**, media leaks revealed proposals from a national commission to allow more immigration for non-EU skilled workers. Fine by me, said the interior minister, Otto Schily. Not by us, said many voters. The Christian Democrats faced both ways.

AP

Silvio Berlusconi took office as Italy's prime minister. His number two: the post-fascist National Alliance's Gianfranco Fini. A

ministry (institutional reform and devolution) for the Northern League's Umberto Bossi. Treasury minister: Giulio Tremonti, a former tax lawyer. Foreign affairs: Renato Ruggiero, once at the WTO.

See article: Italy's new government

Ethnic Albanian rebels in **Macedonia** said they were ready to "demilitarise" but only as part of a peace plan implemented by NATO. War in Macedonia, and NATO's possible role there, was high on the agenda of the Brussels summit of western leaders.

See article: Fear of civil war in Macedonia

Africa's past and present

A Belgian court sentenced two Rwandan nuns to 12 and 15 years in prison. A university professor got 12 years and a former government minister 20. They were responsible for helping to murder 7,000 people as part of the genocide in **Rwanda** in 1994. Heavy fighting between the army and rebels was reported in the country's north-west.

See article: Prosecuting war crimes

Berbers continued their protest against the Algerian government with a huge demonstration in Algiers.

Religious rights

In another battle linked to America's separation of church and state, the Supreme Court decided to allow the opening of **American schools** to religious groups for after-hours meetings.

A crowd of 4,000 coca farmers and labourers looted a town in **Colombia**, in a protest at a United States-backed campaign of aerial spraying of drug crops.

See article: Colombia's drug war

At least 39 people were killed, and thousands evacuated from their homes, by landslides and flooding after days of heavy rain in **Ecuador**.

EPA

Asian anxieties

A Muslim gang holding **hostages** in Basilan, an island in the Philippines, said they had beheaded an American in retaliation for an army attack.

North Korea agreed to a South Korean plan to promote tourism between the two countries. The United States opened talks with the North on security matters.

See article: Talking to North Korea

At least 1,000 people have been executed in **China** so far this year as part of its “strike hard” campaign against crime.

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Inequality

Does inequality matter?

Jun 14th 2001
From The Economist print edition

The new rich may worry about envy, but everyone should worry about poverty

"IT'S the same the whole world over, It's the poor wot gets the blame. It's the rich wot gets the pleasure..." What would the have-nots who penned this lament long ago make of today's world?

There are more rich people than ever before, including some 7m millionaires, and over 400 billionaires. From sipping champagne to taking trips into space, they are getting plenty of pleasure—though as our survey of the new rich in this issue shows, these sad souls have worries, too, not least about the damaging effect their wealth may have on their children. As for the poor, the gap between them and the rich is rising, even in the industrialised countries where for much of the 20th century the gap had narrowed. In America, between 1979 and 1997 the average income of the richest fifth of the population jumped from nine times the income of the poorest fifth to around 15 times. In 1999, British income inequality reached its widest level in 40 years.

That was then, you (or your financial adviser) might say, but this is now and the rich are getting a little poorer once more. Share prices have fallen and much of the industrialised world is heading either for recession or for slower growth. At such times, inequality of wealth tends to narrow, though not necessarily that of incomes. But such times also tend to be those when anger about inequality comes to the fore, and starts to have political and social consequences. For in good economic times, even the poor feel better off. In bad ones, the rich may lose the most money but the poor lose their jobs, their houses, even their families. And then their acceptance of the way the system works?

Questions of justice

That, certainly, is the danger. But how much should people (rich or not-rich) worry about it, these days? In the past, in many countries periods of the greatest widening of inequality coincided, more or less, with periods of democratic reform, as the franchise was extended and the discontented thus gained a channel through which to express their ire. That is no longer necessary. Yet although democracy may well mean that a backlash by the less-well-off will not become literally explosive, there are still plenty of ways in which it could be harmful. Past backlashes have, for example, been bought off through trade protectionism, job-guarantee schemes, extending welfare benefits even to the middle classes and, most notoriously, draconian taxation of the wealthy. All such measures sap an economy's strength and make everyone worse off.

The first question to ask about inequality is this, however: If the have-nots are angry about it, are they right to be? In societies where advancement is on merit and seemingly open to everyone, regardless of class, race, creed or sex, unequal outcomes ought not to be a cause for concern. No one thinks it outrageous that Tiger Woods is the best golfer in the world and rich to boot (see article); we all had the chance to do what he did, but he had the skill and personality. Nor should it be thought outrageous that Bill Gates has made so much money. But where opportunities are not genuinely equal, governments must do what they can to make them so, chiefly by improving public education and ensuring it is open to all.

There is, though, a second way in which anger about inequality could be justified even if opportunities were equal and education were both universal and universally good. It is when power, even power initially gained in a meritocratic way, is abused to raise prices or exclude competitors. That, in a previous backlash, is what gave rise to antitrust laws in America and elsewhere, as governments sought to

restrain monopolies and cartels. Difficult economic times, for companies and for consumers, often give rise to accusations of gouging. The temptation at such moments is for governments to be kinder to companies, for fear of job losses. When genuine abuse occurs, however, that is the wrong reaction.

This issue of abuse of power could also apply to individuals. Resentment at "fat-cat" salaries for bosses has been strikingly muted during the boom years. Partly this reflected a new realism about capitalism, but it was also helped by the fact that everyone was becoming better off. In Britain, the poorest fifth enjoyed real annual income growth of 1.9% under John Major and 1.4% under Tony Blair. In America, the average real income of the poorest fifth fell by 3% during 1979-97, but it has since also moved into positive territory, jumping by 5.4% in 1999 alone. Yet during a recession, companies cut costs, which mainly means firing people.

Resentment at "fat-cat" salaries for bosses has been strikingly muted during the boom years.

As Hemingway might have said when Scott Fitzgerald said the very rich "are different from you and me": "Yes, they get three years' salary and a protected pension and fully-compensated options when they lose their job. I get a month's notice and a black plastic bag." There will be little that governments can do about resentment at the different treatment given to sacked bosses and to sacked workers, but companies themselves—especially their shareholders—should pay heed. Unjust and unequal treatment is poor corporate governance and, in the longer term, is likely to hurt productivity.

...but really of poverty

Liberal democracies and well-run companies ought to be able to find ways to deal with any justified grievances about inequality, and to win the argument against unjustified ones. There is, though, a bigger problem that exists regardless of the gap between rich and poor, but is made starker as a result of it: pure, sheer poverty. Unlike inequality between the few haves and the many have-lesses, this is not readily channelled and defused by democracy, for the truly poor, the underclass, are a small minority. Their interests risk having no democratic means of expression, and can easily be overlooked.

Helping the poor, the truly poor, is a much worthier goal than merely narrowing inequalities. If the rich get poorer thanks to high taxation, some people may feel pleased but few are better off. If the poor get richer, however, the whole country will benefit. Focusing resources and policy on poverty would be worthwhile simply on humanitarian grounds. But also, the disadvantages of growing up in extreme poverty pose a challenge to a belief in equality of opportunity. And helping the underclass rejoin society is in the interests of all.

The main task here is for governments: to provide a proper welfare safety net; to provide and protect public education in the poorest areas; to provide remedial training and schooling; to provide adequate incentives to help the poor get back into (or just get into) work through which they can support themselves. Yet today's many rich individuals can also play a role.

For if they are wise, the rich will behave in ways that help to reassure the rest of the population that rising inequality is not, by itself, a problem. The rich of Victorian Britain helped build great municipal buildings and galleries for art and science. The rich of early 20th-century America used philanthropy to distribute some of their wealth, salving their consciences as well as defusing some of the criticism. Today's rich would do well to follow that example. America's new rich are already beginning to do so, but mostly (with Mr Gates a notable exception) on a small scale. Their compatriots, and the rich elsewhere, ought now to do more. The more they give away to help the poor, the less anybody else will care that the rich have so much money in the first place. And, who knows, it might even turn out that philanthropy is wot gives the rich pleasure.

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After Iran's election

Make haste slowly

Jun 14th 2001
From The Economist print edition

Splits in Iran's reformist and conservative camps point to a modest pro-change consensus

EPA

AFTER sweeping to victory with 77% of the vote, will Muhammad Khatami be able to do more to civilise Iran's clerical regime this time than in his jerky, hobbled first term? Hobbled, because in Iran the elected president, whoever he may be, comes a poor second to the appointed-for-life supreme leader. The more radical steps taken by the reformists last time were promptly reversed by the conservative cohorts gathered round Ayatollah Ali Khamenei. Although most Iranians have now demonstrated their desire for change, to achieve steady progress Mr Khatami and Mr Khamenei will have to work together. With both the reformist and conservative camps split, this should not be impossible.

Would-be reformers of all stamps voted for Mr Khatami since the illiberal rules of the game did not allow the bolder among them to put forward a more adventurous candidate. But expectations of change over the past four years have bred wider ambitions: radicals now look to democratic pluralism, if not to western liberalism. They want to change the country's constitutional structure, limiting the power of the supreme leader and the various councils he controls. Gradualists, Mr Khatami among them, would preserve the strict clerical framework of the Islamic republic, but strive to loosen the social and political restrictions within it.

Likewise, the conservatives are divided between those who fight tooth and nail against all change, and those, a growing number, who have come to accept that a degree of softening is inevitable. The question is where Mr Khamenei himself stands. Not having the personal authority or theological erudition of his predecessor, the late Ayatollah Khomeini, the current supreme leader, though constitutionally supreme, is vulnerable to pressure from those he leads, and particularly from hardline clerical heavies. But there have been signs that his own inclination bends him towards the centrists.

Caution will be repugnant to radical reformers after their famous victory. But it may be salutary to remember the demise of the heady optimism that briefly flourished after the reformists' victory in the parliamentary election a year ago. Almost at once, the reformers were slapped down by a conservative establishment, which controls the judiciary and much else too. The attempt to breathe life into press freedom was stifled, with newspapers banned and journalists jailed. Reform, which had seemed to take a leap forward, was pushed back.

Part of the world again

Outsiders mainly take note of these backward steps: the cruel imprisonment of student protesters, the occasional barbarism, the stridency of anti-American and anti-Israeli statements. But, in spite of all this, Iran has somehow at the same time become a more decent place in which to live, and a safer place for others to live beside. People are far freer than they were before Mr Khatami's first election to express their opinions, to live ordinary lives, to entertain and inform themselves. Economically, life remains harsh, and politically it is still constrained. But socially the improvement has been vast.

No less important, Iran has been reintegrated into the world. Its support of worldwide terrorism has been reined in, even though a few dreadful question-marks remain. It is no longer a rogue state except in American (and Israeli) eyes; America's unilateral sanctions, recently renewed, look anachronistic, the bar to any resumption of normal bilateral relations. Moreover, under Mr Khatami's presidency, Iran has largely mended its fences with the Arab world—except Iraq, where the armed Iranian opposition is based.

Almost all Iranians, except the most hardline fringe, now seem prepared to tolerate a degree of reform, although, after the bloody years of war and revolution, few within the country have any appetite for violent upheaval. Modest change is no clarion call. But if pursued steadily, by Iran's dual leadership, it would probably be an improvement on the bursts of speed, and the jolting stops, of the past four years.

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America and the Koreas

Off to a new start

Jun 14th 2001
From The Economist print edition

Assuming North Korea is ready for a real reduction in tension

Get article background

Reuters

WHEN the leaders of divided Korea met face-to-face for the first time a year ago, there was hope that at last the ice might be chipped from the cold war's final frontier in Asia. But the subsequent thaw, never very quick, then turned to chill again. President George Bush's decision that contacts should resume this week between American and North Korean officials on a "comprehensive" range of issues is expected to breathe some renewed warmth into North-South Korean diplomacy too. South Korea's president, Kim Dae Jung, is hoping that Kim Jong Il, his northern counterpart, will soon pay his promised return visit to Seoul, the South Korean capital. But a genuine thaw will still be a long time coming.

Mr Bush has picked out the right issues: North Korea's missile programme, its nuclear dabbling and the vast size of its armed forces. America, he says, will be ready to respond with aid, trade and an easing of sanctions if the northern Mr Kim demonstrates a verifiable willingness to reduce the threat posed by these features of his rule. But will negotiating on America's terms, rather than picking a fight on his own terms, appeal to Mr Kim? Over the past decade he has specialised in provocative behaviour—trying to hoodwink international inspectors about the amount of bomb-making plutonium he has produced, firing off increasingly long-range missiles and selling weapons to any other dubious regime with the cash to buy. All this has brought rewards in the form of food, fuel and other goodies, as outsiders, including America, have sought to buy off what they feared might be worse behaviour to come.

Mr Bush is right to try to break this dangerous cycle. But it will not be easy. South Korea is nervous that he is asking too much. With American encouragement, it has tried in the past to pin North Korea down to military confidence-building measures, but has got nowhere. It also worries that it will be sidelined if America and North Korea make real progress on security issues. Such concerns can make it hard to keep South Korean and American diplomacy in step, a problem that in the past North Korea has gleefully exploited. What South Korea can offer North Korea is lots more aid and investment, something that until now the southern Mr Kim has been inclined to do for little real return. But an aid package worth paying for—a comprehensive one that might really make a difference to failing North Korea—needs to attend equally comprehensively to the threat that North Korea poses to all. Co-ordination of policy between South Korea and America is thus vital.

After sunshine, twilight?

The North likes to think it holds some high cards—its missile sales, its threats to restart plutonium production—but over the past year it has missed a trick. A year ago the southern Mr Kim's "sunshine policy"—involving offers of aid for the North in the hope of a genuine process of reconciliation—was controversial, but three out of five South Koreans were ready to give it the benefit of the doubt. A year of disappointments later, however, barely one in five supports it. The South's economy is also less buoyant. Its president, limited to a single term, is already losing influence before next year's election.

Both America and South Korea are thus likely to want to drive a harder bargain than the northern Mr Kim is used to. South Korean, American and Japanese aid will still be available, but in return only for a genuine reduction in tension. It is the best offer he is likely to get. He would be wise to take it.

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Biological Weapons Convention

Stop the clock, support the ban

Jun 14th 2001
From The Economist print edition

Don't make the quick the enemy of the good

IS THE century that was pockmarked by the tank and the atomic bomb to be followed by one blighted by the test-tube? Until now arms control has meant curbing numbers of countable tanks, ships, aircraft and bombs, or monitoring mostly prominent events, such as nuclear tests and missile firings, or even at a stretch tracking suspiciously large quantities of harmful chemicals. But the task of controlling biological-warfare agents—like the horrifying weapons they can be made into—makes the hair stand on end.

With the wrong knowledge, test-tube-sized quantities of bacteria, toxins and viruses could spread plague or smallpox, two of history's most virulent killers; or wipe out animal stocks with foot-and-mouth disease or swine fever; or destroy crops with rusts and blights. Marry this to modern biotechnology and it may be possible eventually to direct these easily-hidden horrors at a particular group, thereby removing a deterrent to the use of such weapons: their unpredictability.

All the more troubling, then, that the 1972 Biological and Toxin Weapons Convention—known as the BWC—still has no means to monitor its sweeping ban on the development, production, stockpiling or acquisition of biological warfare agents. Thirty years ago there was no sensible way to do so. A new "compliance" protocol was due to be presented to a five-yearly BWC review this November. But the effort is faltering.

Since the next shot in the battle over the protocol is likely to come from the United States, where the Bush administration has made no secret of its unhappiness with some of its provisions, America will be an easy target for a finger-pointing row at the next, supposedly final, drafting session next month. Better for those who want to curb the biological menace—not even all BWC-signers do (see article)—to avoid a bust-up and find ways to build on the work done so far. For, if this protocol falls, there will be plenty of blame to spread around.

One country on which to spread it will be Russia, which for years maintained a vast illegal biological-weapons establishment, despite being a depository power for the BWC. It is trying to narrow the blanket biological ban in ways that will allow some research it has never quite stopped. Another blame-worthy country is China, which has no wish to admit snoopers to its labs and recently delivered a fierce attack on the draft protocol. Or blame Germany and Japan for wanting too many commercially-inspired restrictions on inspections.

And by all means blame America. It, too, has wanted to limit inspections to protect confidential business information in a lucrative industry. Yet its own inspection trials in 1995 and 1996 raised concerns about the limits being put on some sorts of visits (those aiming to clear up anomalies in declarations of work being done, not the tougher inspections to be carried out when actual wrong-doing is suspected). These could not clear the good guys, let alone snag the bad guys, making them worse than useless. Yet the Clinton administration did nothing. Some dispute the American results, but even some protocol supporters acknowledge these bits of the rules are weak. Inspections need to provide answers, not just more questions.

The purpose of the protocol has never been "verification" of the precise sort that can be applied to tanks or nuclear tests. In the biological business, under a sinister regime every brewery or yogurt maker could be up to no good. Rather, the aim is to enable companies and countries to demonstrate compliance, while using the process of declarations, visits and the close tracking of outbreaks of disease to make

cheating harder.

Some of the protocol's critics in America are pushing to drop it entirely or renegotiate it all. Like the convention itself, it includes words they dislike about encouraging legitimate research and trade. But without these, many countries simply would not sign. Attempting a sweeping reformulation would thus scupper the entire effort. Other governments are keen to adopt a protocol in November no matter what.

Inspect, or be damned

A better approach would be to stop the clock and set a limited period in which to tinker with the protocol's inspection rules so as to produce better results. Such a proposal from America—it's broke here, so let's work to fix it—combined with wording allowing for the adoption of new and better verification techniques in the future, could produce a protocol really worth having. In the biological nether world, reliable information will be well nigh impossible to get without some international means to gather it and investigate it properly. If this opportunity is tossed away, it will not easily come again.

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Climate change

A warm reception

Jun 14th 2001
From The Economist print edition

George Bush needs to come up with a clearer policy on global warming

Get article background

Reuters

WHY is George Bush so reluctant to do anything serious about global warming? Surely not, as some cynics suggest, because he is in the pocket of America's fossil-fuel industry. Yet his action (or rather inaction) in this area inevitably makes such scepticism harder to counter.

In his first few months in office, Mr Bush sparked huge rows at home by backtracking on a campaign promise to curb emissions of carbon dioxide, and abroad by reiterating his opposition to the Kyoto Protocol, a United Nations treaty on climate change that has been in the works since his father signed an earlier UN treaty in 1992. In defusing those rows, his advisers cooed that they were opposed only to Kyoto—not to all action on global warming. They promised to come up with a credible alternative quickly. Time is now pressing—the next round of negotiations on climate change will take place next month in Bonn—and yet the Bush team has not come up with even an outline of a plan.

This inaction comes even though the case for doing something to tackle global warming is growing stronger. Unwilling to accept the opinion of international scientists, Mr Bush asked his country's leading climate experts to produce a red-blooded, all-American analysis. That panel has just produced its report, and, despite the many uncertainties, its conclusion is crystal clear: global warming is real, man's role in it is real and the dangers it poses are serious (see article).

Mr Bush duly unveiled a new policy this week, but it was at once devoid of substance and full of contradictions. Although he acknowledged in passing the chief conclusion of that report, that the threat from global warming is genuine, most of his statement dwelt on the lingering uncertainties. Although he professed faith in a global approach under the UN umbrella, he repeated his view that the Kyoto pact was "fatally flawed" without offering ideas for how to fix it. And, although he accepted that the United States had some responsibility to act, he refused to do so unless India and China do too—even though his rich, energy-guzzling country has contributed far more to global warming than have those dirt-poor countries.

The most curious contradiction came on the question of whether to act now. The president declared that he is "committed to a leadership role on the issue of climate change", but the only concrete action he could come up with was a promise of more money for science and technology. There is indeed a need for continuing research into a problem as potentially catastrophic as climate change; but that does not justify demanding repeated scientific proof that the problem exists before being ready to take any substantial action to deal with it.

Kill Kyoto to save it?

All this is not to say that Mr Bush should now fall meekly into line behind the Europeans in embracing Kyoto, warts and all. Indeed, there is much to criticise in the Europeans' hysterical and often hypocritical stance. Their posturing was the main reason why the previous round of Kyoto negotiations collapsed back in November. The EU rejected sensible proposals by the Clinton administration to use market mechanisms that would have ensured that the pact was implemented as flexibly and cheaply as possible—and it did so despite knowing that Mr Bush was likely to be the next president.

Referring to the Europeans, Mr Bush declared this week that "we have a different approach, but we have

the same goals." If that is true, the conclusion should be obvious: that the right policy is to fix the flaws in Kyoto, not to junk it. As an approach to global warming, Kyoto has compelling strengths that make it worth saving. It is global, its architecture is flexible and, like the GATT process of trade liberalisation, it is designed for continuous renewal and review. Such a robust approach can adapt as climate-change science improves.

Europe and America should therefore build on the decade's worth of goodwill, hard-won compromise and intellectual capital poured into the Kyoto framework. They must use the talks in Bonn to reconsider the treaty's unrealistic and arbitrary set of emissions targets and timetables. That could produce a deal with more realistic targets, and a less front-loaded timetable. Extending the timetable for the first emissions targets, now only a decade, would hugely reduce the cost of meeting them. And it should also persuade developing countries to accept future cuts in emissions, which would make the pact more credible as well as more acceptable to the American Senate. Provided these changes are made, Mr Bush's blunt rejection of the Kyoto Protocol in March could even turn out to have been beneficial—but he does not have much time left in which to prove his case.

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The European Union

Can it work and be popular?

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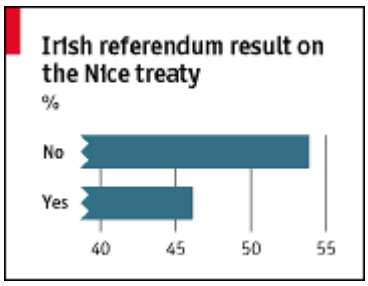
From The Economist print edition

Or can it work if it is not popular?

IT'S a nice dilemma. Suppose you support the enlargement of the European Union, as *The Economist* does, and suppose you also support, as we do, the notion that the EU should be a democratic enterprise that pays attention to the views of its people and does not just arrogantly present them with *faits accomplis*. How then do you respond to a referendum in which Ireland's voters roundly say no to a treaty, negotiated by their government, which paves the way for the Union's expansion? Without Ireland's approval, the Nice treaty signed last December by the governments of all 15 of the EU's existing members will fail, and the current effort to admit a dozen or more newcomers will be thrown into confusion. But don't the voters deserve to be heard?



No, is the customary answer from the visionaries who run the Union. If some voters in their unwisdom give the "wrong" answer to a question put to them, the question must be put again until they get the answer "right". That is what happened when the Danes were consulted about the Maastricht treaty in June 1992 and had the temerity to say no. A year later Denmark voted again, and this time it gave a decisive yes. In fairness, the naysayers had been heard: on the second occasion, they were told that Denmark would not, after all, have to take part in Maastricht's common currency, common defence, common citizenship or joint policies on home affairs, which were obligatory for all other countries, though Britain too was exempted from the currency. A similar tactic of opt-out-and-reconsider is the obvious one to offer the Irish now, allowing Ireland to exclude itself from any EU military ventures it does not like, and the expansion of the club to go ahead as planned. It would all be quite democratic.

But it would still be a tactic. A strategy, a democratic strategy, would be rather different. Instead of treating voters' participation as a tiresome complication that usually stands in the way of concerted EU action, it would positively welcome their involvement. Indeed, it would recognise that, if the Union takes its citizens' approval for granted, it runs an increasing risk of coming seriously unstuck, for it is not just in Ireland that Europeans are showing signs of uppitiness. In their present mood, several other nations—the Austrians, the Spanish, perhaps even the French—might reject the Nice treaty, given the chance. Better, surely, to make politicians sell their treaties to the voters and win majority approval before hostility to, say, Maastricht or Nice turns people against the EU in its entirety.

And what if the voters say no? Is the business of 370m people in 14 countries to be halted by a handful in just Ireland (population 3.7m), or maybe Luxembourg (422,000)? Unfortunately, that can happen already. Indeed, enlargement could well anyway be thwarted if Greece does not get its way over the admission of Cyprus: each member has a veto in treaty matters. So why not get rid of the power of veto, and put in its place a requirement that treaty changes should require the assent only of three-quarters or more of the countries in the Union, perhaps weighted by population? The exact way in which countries choose to secure their citizens' approval should be left to the countries themselves, though for most a referendum would seem to be the best measure for any constitutional change. A country that could not live with a treaty thus introduced or amended would be free to leave the Union.

Better to opt out than to veto

Not so fast, you may object. Such an arrangement would enable a majority to force just one member—Britain, say, for the sake of a purely hypothetical example—to choose between (hypothetically again) the euro and withdrawal from the EU altogether. Outrageous, unthinkable.

Yet it need not be so: Britain could be, and indeed is, allowed simply to opt out—a right which is given

grudgingly at present, but which should be extended whenever a single member's reluctance to join in does nothing to hinder the others going ahead on their own. If a few or even a lot of countries want to set up a common currency, or make an agreement allowing unfettered cross-border travel, let them do so. The non-participation of other countries need not stand in their way.

On the other hand, if a single refusenik tries to prevent genuine common action, such as the admission of new members, it should be politely told to lump it or leave. Otherwise today's Irish or Greek problem will become tomorrow's Estonian, Latvian or Slovenian problem: a country of a million or two people thwarting the wishes of, and perhaps holding to ransom, 480m. Even if, perish the prospect, the current effort at enlargement should fail, it is clear that the Union will have to adopt three principles it still seems to dislike: more opt-outs, more majority voting and more popular involvement. The alternative will be paralysis, or death by loss of legitimacy.

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Letters

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From The Economist print edition

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Ever larger Union?

SIR – Your survey on European Union enlargement (May 19th) understates the historical and moral case for Polish membership. Historically, Poland has always been part of Europe. Nor was it "only the tragic accident of the cold war" that stopped Poland creating a democratic political system and free-market economy. Churchill and Roosevelt agreed to let Stalin install a Soviet-trained, communist puppet government. Poland's suffering under German and Soviet occupation also stemmed from allied betrayal. France and Britain agreed to deny military help against Germany.

Poland will meet *acquis communautaire* requirements despite facing far more rigorous conditions than previous members. The EU would do well to quit its fainthearted and needless procrastination; the Poles will come through with flying colours. Then again, this may be a concern for some current members.

Gene Sokolowski
Burke, Virginia

SIR – You assert that structural funds merely redistribute income to poor EU regions but are not an incentive to development. This is probably correct but your argument in support of this contention is flawed. Differences in the rate of change between regions of a country do not prove that the funds are misguided. It simply indicates that in regions that are catching up fast, other forces are operating (eg, private investment). The real problem is when inequality is intraregional. Big national infrastructure projects do not spread benefits equally. Reforms aimed at benefiting poor regions should be designed "from the inside".

Rafael Caballero
Madrid

SIR – You repeatedly mention a need for precise "objective criteria" for the acceptance or the rejection of EU candidates. This search is useless and unprofitable. Such efforts will tend towards a lowest common denominator, which does not do justice to the complex richness of Europe and its changing interests.

Judged by a criterion of "like us", Turkey, Russia and Ukraine do not belong in the EU. Among the arguments invoked for Turkey's membership are the promotion of human rights, bridling its generals, fostering European commercial interests in Central Asia, keeping fundamentalists in the region at bay, the security of Europe and the safety of oil supplies. While these objectives are of some value, they can be reached through means other than accession and, therefore, without endangering Europe's cohesion.

Anton Smitsendonk
Saint-Cloud, France

SIR – You state that the island of Cyprus is "divided into a Turkish-occupied and a Greek-occupied part". This is incorrect; no part of Cyprus is occupied by Greece. While Turkey occupies approximately 40% of the island of Cyprus—and has done so since 1974 despite United Nations resolutions to withdraw its troops from the island—the remainder is governed by the internationally recognised government of the Republic of Cyprus.

Evangelos Papanastasiou
Dounan Town, Taiwan

Independent intifada

SIR – Your article on Yasser Arafat's lack of control over the Palestinian people is relevant ("Arafat's studied non-interference", June 2nd). Many people, especially in America, believe that Mr Arafat has the power to stop the intifada. Unfortunately, this is not the case.

Most people do not know what it feels like to live under occupation. The Palestinians have been living under Israeli occupation for many years, which is why many have taken to the streets and resorted to violence. The Palestinians are not fighting because they are told to but rather because they want to. This is not a conflict of rational decisions; it is a conflict of passion. Passion cannot be stopped in the way that decisions can.

Unfortunately, much of America's media tend to be pro-Israeli. There would be much more support for the Palestinian cause if more Americans were exposed to their view of the conflict.

Ian Shieh
Wayne, Pennsylvania

Friends across the Atlantic

SIR – I strongly disagree with the jingoistic Richard Sybert (Letters, May 26th), who demands that you stop your examination of my country's love affair with capital punishment, and offer thanks for our having singlehandedly freed the world from tyranny.

A surprising amount of Americans do acknowledge our debt to our European cousins, nay all the peoples of the world, and we welcome their opinions every bit as much as we try to impose ours. Not all of us are handicapped with the same myopia as my countryman, having learned long ago to think with our Syberts rather than our Richards.

Eric Karp
Los Angeles

Argentina's debt

SIR – Unfortunately, your analysis of the Argentina debt swap is inaccurate, and the conclusions on Argentina's fiscal solvency drawn from it are wrong ("Cavallo pawns an uncertain future", June 9th). Contrary to your assertion, Argentina does not pay interest of about 15% on the bonds issued in the recent debt swap. These bonds pay coupon rates between 7% and 12.25%, and more than half of the new debt issued will pay no interest at all during a grace period of five years. Instead, the yield to maturity of the new bonds is in the neighbourhood of 15%, as they have been issued at a discount. But as the old bonds were exchanged at a discount as well, the government does not pay up substantially for the new debt.

Overall, the debt exchange was a great success. That said, lack of growth and political tensions could still push Argentina over the cliff.

Christian Kopf
Frankfurt

E-conomics

SIR – In attributing the lack of profitability of most Internet businesses to "west coast hippies" and their simplistic aphorisms, you ignore the economics behind the Internet ("Off with their beards", June 2nd). Hippies do not have to tell companies with relatively high fixed costs and low marginal costs how to behave, the market will do it just as well. A glance at the travails of long-distance phone carriers and airlines proves that point.

Kevin Cassidy
New York

America's rebellious north

SIR – In 30 years of living in the state I have never been so proud to be a Vermonter ("What one man can do", May 26th). Jim Jeffords's abandonment of the Republican Party bids fair to help slow or divert the Bush-Lott-Hastert-driven mudslide toward domestic meanness, international isolationism and missile-shield madness. And now, let us hope that George Bush feels the pain of a British general, John Burgoyne. On his fateful march to Saratoga and disaster in 1777, Burgoyne commented that "Vermont is a country which abounds in the most active and rebellious race on the continent and hangs like a gathering storm on my left."

Bill Mares
Burlington, Vermont

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Economist.com SPECIAL

Judging genocide

Jun 14th 2001 | ARUSHA AND THE HAGUE
From The Economist print edition

AP

Getting justice for the worst war crimes may be impossible. But two United Nations courts are trying, and a court in Belgium has just joined in

Get article background

“WE DON’T have a place to put our robes on. There’s no place to hang up our coats, or to lay down our briefcases! We have been mistreated by this tribunal!” The speaker is a New York defence lawyer; the scene is the courtroom at Arusha in Tanzania. The trials taking place here, before a United Nations tribunal, are for the murder of hundreds of thousands of people in neighbouring Rwanda in 1994. Much more time and energy, in this dusty town at the foot of Mount Kilimanjaro, seems to be consumed with complaints about how badly the court works.

On June 8th the International Crisis Group (ICG), a think-tank based in Brussels, added its voice to the chorus. The Rwanda tribunal, after seven years of life and with an annual budget of $90m, was hopelessly behind schedule, “bogged down by incompetence and bureaucratic infighting”. Five of its nine judges had spent more than 18 months without hearing a substantial case. The only case of consequence heard since July 1999, that of Ignace Bagilishema, a former mayor in western Rwanda, ended on June 7th with his acquittal. Mr Bagilishema, who had been accused of being instrumental in the deaths of 45,000 Tutsis, was let off because of insufficient evidence. Perhaps the verdict was correct; but with confidence in the court so low, many are doubtful that justice has been done.

External difficulties are certainly distracting. Arusha is ill-equipped to host 800 UN staff, from over 80 countries, and swarms of defence lawyers. Power cuts are so frequent that the tribunal relies on its own generator. At first, Arusha’s small banks could not cope with the large dollar salaries of UN staff. Although it has a conference centre, and is well-off compared with the rest of Tanzania, the town has few hotels, hospitals or shops. Setting up a tribunal there was a matter of improvisation or making do. The court’s website, for example, was knocked together at a dollar-an-hour Internet café in a local shop.

In 1997, an internal UN report exposed “the most troubling deficiencies” in the finance section of the tribunal. Although these have been rectified, other problems remain. In May, seven prosecution lawyers were told by the chief prosecutor that they had been sacked for “professional incompetence” and for being “absorbed in their own narrow self-interest”.

Yet in 1998 the court at Arusha managed to convict the Rwandan prime minister, Jean Kambanda, the first head of government to be convicted of genocide and crimes against humanity. This, says Kingsley Moghalu, a tribunal spokesman, set a precedent for the indictments of Chile’s General Augusto Pinochet and Yugoslavia’s ex-president, Slobodan Milosevic, by other legal bodies. And suspects are still being arrested. At the end of April Kenyan police arrested a former Anglican bishop, Samuel Musabyimana, who is accused of genocide and of paying militiamen to kill Tutsis.

Mr Moghalu also points out that the Arusha tribunal has broken new ground in

international law. It has established that rape can legally be considered an aspect of genocide. The first trial of a woman charged with genocide (another minister from the old Rwandan government) is due to begin soon. The court is trying to develop a concept of restitutive justice by assisting victims of crimes, usually witnesses and their families.

The Arusha tribunal has broken new ground in international law

Yet there is no denying that Arusha is slow; painfully so. Seven years ago, at least 800,000 Tutsis and a relatively few Hutus were killed by machete-wielding countrymen in less than two months; it may have been the fastest-ever slaughter on such a scale. Just 63 people have been charged in connection with those crimes. Of those, 45 have been caught; nine are on trial, and 27 more are waiting to be tried. Only eight people have been convicted, and these have not yet heard their sentences.

The speedier Belgians

With everything moving so slowly, the chances of convicting large numbers of people at Arusha are slim. The ICG study concludes that "there is a serious risk that those already in custody will be released because they have been held for too long without trial." Meanwhile, the new Rwandan government across the border views the proceedings with impatience. It keeps some 130,000 genocide suspects in its own prisons, and in 1998 executed for that crime 22 people, all of them convicted in a sub-standard court.

On June 8th, however—the very day of the scathing ICG report—two Roman Catholic nuns were found guilty in a different court, thousands of miles away, of complicity in the Rwandan genocide. Their trial had lasted a mere two months. Sister Maria and Sister Gertrude had handed over to their killers up to 7,000 Tutsis who were sheltering in their convent; later, they provided petrol so that militiamen could set fire to a barn in which about 500 Tutsis had taken refuge. They were sentenced to prison terms of 12 and 15 years by a jury sitting not in Africa, but in Belgium. It was the first time that a jury of citizens from one country had judged defendants for war crimes committed in another.

It may not, however, be the last. Belgium is a signatory to a law, passed seven years ago, that allows its courts to hear cases of alleged atrocities even if these occurred abroad. Its interest in the Rwandan case is that Belgium was the former colonial power in Rwanda, and that the nuns had fled there after the genocide. The verdict has heartened many; if more countries do as Belgium has done, perpetrators of war crimes will know they cannot hide from the long arm of justice.

AP

Nuns took part, too

Should the practice be expanded? Perhaps so, if Arusha is the alternative. But the other UN war-crimes tribunal, sitting in The Hague in the Netherlands, gives a different impression. It was created in 1993, a year before Arusha, and, like that tribunal, was seen at first as an effort by western countries to soothe their own consciences about the Balkans and elsewhere, because they had not intervened to stop the atrocities. But it has grown from similarly shaky beginnings to become respected.

The crimes examined there, though committed on a smaller scale than those in Rwanda, are just as brutal—genocide, crimes against humanity, contravention of the rules of war. Although the tribunal has not yet convicted anyone as highly placed as a prime minister, 100 people have been publicly indicted. (The chief prosecutor talks of doubling that number, and more may already have been indicted in secret, meaning that their names have not been revealed.) Thirty-eight people are awaiting trial and proceedings have started against 41, although just four people are actually serving sentences. So far, over $470m has been spent on this court from its allocated UN budget alone.

The Hague tribunal clearly has advantages over its sister tribunal in Tanzania. It has a slightly larger budget from the UN and a few more staff (1,100 at The Hague, 800 at Arusha). But the European court gets roughly as much money again in one-off bilateral payments or gifts in kind, such as Britain's gift, a few years ago, of a newly-furnished courtroom. And the Dutch government provides back-up, such as security, that the Tanzanian government cannot provide in Arusha.

There are also more resources available to the prosecution at The Hague. Arrests are made mostly by NATO troops in the Balkans. For Arusha, suspects are picked up when police, mostly in French-speaking

west African countries, happen to spot them. Arusha depends mostly on witnesses for evidence, many of them illiterate farmers who could not record their impressions at the time. The Hague enjoys intelligence intercepts from western armies, satellite photographs and other high-tech methods of collecting more durable evidence.

Take, for example, the trial of Radislav Krstic, a one-legged Serb general who is accused of killing 8,000 Bosnian Muslims in Srebrenica in July 1995. The case against him rests partly on photographs of vehicles, buildings and soldiers in and around Srebrenica which were taken from NATO planes and satellites. The prosecution has presented over 900 exhibits, including those photographs and evidence gathered by spies, as well as over 100 witnesses. Arusha has nothing like this.

The best lawyers and judges are more willing to work in Dutch comfort than to go to down-at-heel Tanzania

The best lawyers and judges are also more willing to work in Dutch comfort than to go to down-at-heel Tanzania. Carla Del Ponte, a former Swiss attorney-general with a reputation for hunting down members of the Russian mafia, is the chief prosecutor for both tribunals. She spends three weeks in every two months in Arusha, and finds it exhausting. “With Rwanda,” she admits, “it is difficult to find people who will stay down there.”

Fishing for the biggest

Neither tribunal, however valiant its efforts, could provide full justice for these horrific crimes. As with the Nazis who were tried at Nuremberg, it is clear that many thousands more people were responsible for all sorts of crimes than can actually be put on trial.

In Rwanda, the killers were mostly ordinary peasants who joined “the work”, a communal activity for Hutus, who were all expected to take part in the killing. Decent Hutus who refused were often killed themselves. In the Balkans, neighbours turned on each other with a vengeance. Since no more than a tiny fraction of the guilty can be tried, is justice possible at all?

Ms Del Ponte’s answer is simple: grab the people who are most responsible. In Arusha, trials are due this year of a pastor, several politicians and military officers. The Hague tribunal is also hunting down more senior people. Biljana Plavsic, once president of the Serb part of Bosnia, surrendered to the court in January, and will stand trial for genocide and other crimes. Radovan Karadzic and Ratko Mladic, two leading Serbs, have been indicted on similar charges.

The trial of one man would crown the efforts of The Hague. Pasted to the wall of Ms Del Ponte’s office is a wild-west “Wanted” poster, offering $5m for the arrest and delivery of Mr Milosevic, the main architect of the Balkan wars. Mr Milosevic was publicly indicted during the Kosovo war in 1999, and Ms Del Ponte makes no secret of her eagerness to bring him to trial. “I am waiting for Milosevic. I will go in court then, yes!” she cries, banging the table with her fist.

She may have to wait. Mr Milosevic was arrested in Belgrade in April; Yugoslavia’s new president, Vojislav Kostunica, would prefer to have him tried for war crimes at home first, although a new law would allow co-operation with the court in The Hague. Staff at the war-crimes tribunal are confident that outside pressure will eventually bear fruit. The news, released on June 3rd, that the Belgrade authorities were examining bodies from several mass graves in Serbia has increased speculation that Serbs are being prepared for Mr Milosevic’s journey to The Hague. “There is no question [about] the transfer of Milosevic,” says one official. “It is just a question of when they will do it.”

AP

Uncovering the past in Serbia

The justice of the victors?

Even if a tribunal is able to put the worst offenders on trial, some question whether justice results. On one reckoning, there is no punishment severe enough to fit crimes like genocide. UN courts cannot sentence anyone to death, and UN-approved prisons are usually tolerable places. Not much of a deterrent, therefore, for those committing crimes in the heat of a war. This is a particular problem in

Arusha, where prisoners live in greater comfort than surviving victims of the genocide. The Arusha tribunal is now trying to find African prisons (in Mali, Swaziland and elsewhere) which meet international standards but are still seen as punishment.

A greater problem is that war-crimes tribunals are perceived as nothing more than revenge on the victor's part. Serbs complain that The Hague tribunal is a western plot, directed mainly at them. Those on trial in Arusha feel the same.

In general, victors in war escape facing justice. The Nuremberg trials after the second world war did not consider whether British or American bombing raids against civilians were war crimes. Russia's soldiers are most unlikely to face a war-crimes court over the murder and torture of Chechens. The Hague tribunal did investigate NATO's bombing raids on Yugoslavia, but concluded, rightly or wrongly, that there was no reason to prosecute.

Critics can therefore argue that war-crimes courts are doubly selective: not only are very few people tried, but very few wars are considered for judicial investigation. When justice is so selective and seems driven by political interests, is it justice at all?

Critics can argue that war-crimes courts are doubly selective

This question is being answered, in part, by the proliferation of different tribunals where war crimes can be tried. More UN war-crimes tribunals are in prospect, as is a permanent International Criminal Court. And there remains the example of Belgium: wherever war criminals seek sanctuary, that country can put them on trial. The limitations of Belgium, however, are seen in the case of Mr Milosevic. Where the fish are very big, the tribunal judging them needs international stature.

Recent violence in Burundi, Congo and East Timor has led to demands for dedicated UN tribunals. Atrocities committed by the Khmers Rouges in Cambodia in the 1970s may one day also be examined by a court, perhaps with an international element, although legislation to establish one has stalled in the Cambodian parliament. Members of the military junta in Myanmar are said to worry that they may one day end up in court. Some even argue that Henry Kissinger should be tried for human-rights abuses in Chile, Cambodia and elsewhere during the cold war (so far, he has been called as a witness only).

The most likely third UN tribunal will be one for Sierra Leone, in west Africa. Over ten years, rebels have committed horrific cruelties against civilians in the country. Tens of thousands of people are thought to have been killed—though the slaughter is not technically considered a genocide, since it has not been an effort to kill a whole ethnic group.

Whereas the tribunals for Rwanda and Yugoslavia were set up by the UN's Security Council and are entirely international, the new one will be based on an agreement between the UN and Sierra Leone's government made last October. If money and support can be found ($22m is needed for the first year), Sierra Leone's tribunal will mix local and foreign judges and an international prosecutor. If the war allows, the tribunal will sit in Freetown, the shattered capital. Cash may be the main problem. The Rwandan and Yugoslav tribunals are mostly financed through mandatory fees levied on all UN members, but the Sierra Leonean court will depend on donors.

Sceptics may ask what the use of a third court would be. The brutal fighters in Sierra Leone's war will not be deterred by the threat of prison. The court may interfere with peace efforts, and may drain away resources that would be better spent on ordinary people. But those involved in both the existing tribunals argue that courts provide something extremely valuable: an historical record that atrocities did take place and that victims suffered. Getting that fact established, they say, may help countries like Sierra Leone begin reconciliation and rebuilding.

The other big development, the creation of a permanent International Criminal Court, may answer the allegation that international justice is always the victors' sort. In July 1998, a UN meeting in Rome adopted a statute for the permanent court. So far, 139 countries have signed up to it. Once 60 countries have ratified the necessary legislation (Croatia became the 32nd country to do so, on May 21st), the court will come into existence, possibly within two years.

The world criminal court is likely to be based on the two existing UN tribunals, and will build from precedents and practices established there. It will try only crimes committed after its creation. The stumbling block remains the reluctant United States. President Bill Clinton signed up to the Rome statute just before leaving office, but many suspect that American involvement in the court is

The stumbling block remains the reluctant United States

destructive. The United States demands, for example, a guarantee that American soldiers will never be put on trial, which even its closest allies reject as incompatible with the rule of law.

But, if the new permanent court is to build on the stumbling successes of the two UN tribunals in Arusha and The Hague, it will need as much support as possible from rich countries. If America continues to oppose it, Europe, Canada, Australia and other backers will have to throw their full weight behind it. The two existing tribunals have shown how much political will, money, expertise and sweat is needed to make such courts work.

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George Bush's European tour

A bumpy landing

Jun 14th 2001 | BRUSSELS, MADRID AND GOTHENBURG
From The Economist print edition

On his first visit to their continent, George Bush told European leaders that he is no unilateralist. And that they will just have to get used to it

"EUROPE whole, free and at peace": George Bush's motto for his European policy, repeated endlessly this week, went one better than his father's formulation of "whole and free" (applied to the programme for expanding NATO at the end of the cold war). This deliberate echo of continuity was both reassuring and strange in a trip devoted largely to persuading his allies that the end of the cold war actually requires a radical rethinking of security policy. After six days, five countries, four summit meetings, 22 heads of state, three royal families and umpteen demonstrators protesting against everything from the death penalty to global warming, Mr Bush looked likely to get at least half his aims fulfilled.

As *The Economist* went to press, just as Mr Bush was due to join European Union leaders at Gothenburg, most of the attention had been focused on reactions to the president. That was understandable, given the protesters and the initial hostility of many European governments (especially over America's rejection of the Kyoto climate-change treaty). For most European leaders, this was their first look at Mr Bush. Yet, as one European diplomat in Washington puts it, "perhaps the more interesting question is not what Europeans think of the administration. It is what the administration thinks of Europe."

The administration's emerging European policy covers everything from steel trade and global warming (both topics for the summit with the EU in Gothenburg) to human rights, the Middle East and the Koreas. But, for the moment, it is dominated by nuclear security.

For the past few months, the Bush administration has been wrestling with two versions of a European policy, which are in part differing reactions to the EU's own security ambitions. Nobody in Washington thinks the United States should pull out, of course, or even pull back far. But one strand of opinion—represented by officials in the Pentagon and America-firsters in the Senate—argues that it should withdraw some of its 120,000 troops in Europe, and step back, allowing Europeans to play a bigger role in the day-to-day management of their continent's security. The other—represented by the State Department and the National Security Council—thinks America should continue to act as a European power, committing itself unequivocally to the expansion of NATO and the European Union. Cutting across this divide has been the Bush administration's uncertainty over the EU's first steps towards creating its own reaction force, under the European Security and Defence Policy (ESDP).

The European policy that emerged from Mr Bush's visit appears to resolve the administration's strategic indecision in favour of the Europeanists. In Brussels, Mr Bush came out strongly in favour of a new round of NATO expansion (though without specifying who should join). Lord Robertson, the alliance's secretary-general, said he expects to launch a new round of expansion next year, starting at a summit in Prague. The "zero option" (no one else gets in) is off the table. Mr Bush was expected to be similarly supportive of further EU expansion in Gothenburg.

No less important, Mr Bush went out of his way to soothe inflamed nerves over two touchy points affecting defence. As an earnest of his good faith, Europeans had wanted the president to back his secretary of state's formulation for continued commitment to the Balkans ("in together, out together"), rather than his defence secretary's suggestion that some troops be pulled out. He did so explicitly.

He was equally forthright on the ESDP: "The United States would welcome a capable European force,

properly integrated with NATO, that provides new options for handling crises when NATO chooses not to lead." Clearly, the support is conditional. Equally clearly, American support for ESDP has been evident since Tony Blair's visit to Washington in February. Still, to spell it out again at NATO headquarters was significant, given the uncertainty that existed at the start of the year.

But if Mr Bush avoided any temptation to disengage—the isolationist option—he was no less insistent about pushing what many Europeans see as the "unilateralist option": deploying a missile-defence system in defiance of the Anti-Ballistic Missile (ABM) treaty. Mr Bush called this treaty "a relic of the past". Jacques Chirac of France, in contrast, called it a "pillar" of the framework of strategic balances, while Gerhard Schröder, the German chancellor, insisted that "we are committed to strengthening the arms-control architecture."

Hardly a meeting of minds, you might think—and certainly not something that bodes well for Mr Bush's summit meeting in Slovenia with Russia's Vladimir Putin, whose foreign minister bluntly characterised his government's commitment to the ABM treaty as "categorical and unchanged". Yet the Americans have more cause for satisfaction than this opposition to their policies suggests.

Not for the first time, America has been able to use smaller nations as a counterweight to the more truculent block of Europeans within NATO. Two of the newest members of the alliance, Poland and the Czech Republic, strongly supported missile defence. The Czech president, Vaclav Havel, even claimed that a defensive alliance like NATO has a moral imperative to develop defensive weapons.

And despite the opposition of France and, to a lesser extent, Germany, Mr Bush has done better with other European power-brokers. Spain's Jose Maria Aznar was surprised that the very idea of missile defence should be "disqualified". Tony Blair said "there are highly unstable states developing nuclear arsenals and we have to look at all ways, including missile-defence systems, of countering that threat." Perhaps more significantly, Italy, whose new leader, Silvio Berlusconi, is a keen Atlanticist, expressed guarded support for the idea.

This pro-Bush coalition is no guarantee that European countries will eventually endorse missile defence. Some of their deference may be a diplomatic reluctance to rebuff Mr Bush to his face. The president has also avoided giving adversaries anything concrete to attack. The devil remains in the details—and in Mr Putin's reaction.

At his speech in Warsaw, the culmination of his European tour, Mr Bush was due to compare Europe "whole, free and at peace" with Churchill's iron curtain speech of 1946. At that time, America and Western Europe united in the face of a clear Soviet threat. For all their attempts at agreement this week, America and Europe are far from uniting in the face of the more nebulous threats of the post-Soviet era.

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Timothy McVeigh's execution

Gone, but not forgiven

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The long-planned death of the Oklahoma City bomber changed very little

THE contrast between the events that will forever link Oklahoma City and Terre Haute, Indiana, could not have been greater. The bombing of the federal building in Oklahoma on April 19th, 1995 was sudden, without warning. The execution of the bomber, Timothy McVeigh, in Terre Haute, was choreographed as a slow and detailed ritual. The 168 victims murdered in the blast were scattered amongst the debris: doctors pieced together body parts of children like a jigsaw puzzle to give their parents enough to bury. McVeigh's death was clean, antiseptic and calm.

EPA

McVeigh never even said sorry

But the biggest difference was the reaction. Only a handful of fanatics supported the deaths in Oklahoma. The vast majority of Americans supported McVeigh's execution—despite a chorus of disapproval from overseas and a vociferous debate on the subject in the United States. No execution since that of Gary Gilmore in 1977, which re-opened the current era of capital punishment, has prompted the same degree of interest.

The execution ran less smoothly than it should have done. It was supposed to take place on May 16th. It was postponed to June 11th when the FBI, after more than six requests from McVeigh's lawyers, suddenly found more than 4,000 pages of extra evidence.

Even that date looked optimistic. Although these still-sealed documents apparently contain nothing to contradict McVeigh's boastful confessions, it was widely assumed that his lawyers would be granted more time to study them. The chances of the case dragging on for months (or years) were also helped when McVeigh, given the opportunity to tweak the government further, reversed his earlier wish to speed up his punishment.

He did not succeed. The federal judge in Denver who presided over McVeigh's trial tore into the FBI for its negligence, but ruled that nothing in the last-minute disclosures would exonerate McVeigh. His order allowing the June 11th date to stand was backed by the federal Court of Appeals. Rather than make a futile appeal to the Supreme Court, McVeigh again accepted the sentence.

He spent his last days maintaining his delusion that he was a soldier in a state of war with the federal government. He showed no remorse; his half-apology was largely another justification for the murders. He hand-copied a mawkish 19th-century poem "Invictus" for his final statement but did not, in the end, read it.

For his last meal he ate two pints of mint chocolate-chip ice cream. He slept during the last hours of his life, and hopped up on the gurney just before 7am. After he was strapped in place and the intravenous lines inserted, the witness-room curtains were opened. He made eye contact but said nothing to the witnesses, simply looking at the camera in the ceiling. In Oklahoma City survivors and relatives of the dead saw his face looming before them on a big screen as he defiantly stared at them, dying with his eyes still open. When he was pronounced dead, at 7.14, the transmission ended.

McVeigh's long-term significance in the debate about capital punishment remains to be seen. On the day of his death, the focal point for many people was not Terre Haute but the memorial on the site of the federal building in Oklahoma City where 168 sculpted chairs honour the people whom McVeigh slaughtered. Nineteen of the chairs are smaller than the rest, in memory of the children murdered in their day-care centre. On the edge of the site is the Survivor Elm, a tree damaged but not destroyed in the blast. For the first time in six years, birds have returned to nest in its branches.

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Appointments

The Potemkin administration

Jun 14th 2001 | WASHINGTON, DC
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All the president's men are arriving very slowly—and it is beginning to show

THERE IS nothing like a trip abroad to convey the impression of the might of an American administration. The president is born hither and thither on Air Force One. He is surrounded by a praetorian guard of secret-service agents. The world's press corps hangs on his every word.

But back home in Washington the new administration is far from being a mighty machine. George Bush's plans face gridlock in a newly Democratic Senate. The administration itself is nothing more than a work in progress. Very slow progress. Almost five months after inauguration day just under a quarter of its senior officials have been confirmed in their jobs. Paul Light, of the Brookings Institution, calculates that Mr Bush may not have all his appointees in place until March 2002.

Desperate improvisation is thus the order of the day. The administration makes some use of trusted lieutenants who are awaiting confirmation. But they are strictly limited by law to offering advice. They cannot attend official meetings with interest groups or foreign officials unless escorted by a department official. They cannot even use their dining rooms or car parks, let alone sit in their future offices. The White House also makes some use of people held over from the Clinton regime. But they can hardly be expected to prosecute the Bush agenda with any great enthusiasm. And lower-level people who do not require confirmation are used to do the jobs of their seniors. But, above all, the White House loads mountains of work on the few people who have been confirmed.

Some early cock-ups were probably linked to lack of people

At the height of the China crisis only five of Mr Bush's 47 appointees in the State Department and just two of the Defence Department's 45 appointees were in office. The Department of Education is handling a complex education bill with, to date, just two out of 16 positions filled. The Interior Department is conducting a heated debate about drilling in the Arctic with just one out of 17 positions filled. At the height of the debate over the tax bill, Paul O'Neill, the treasury secretary, had to go to a banking conference in Honolulu because there was nobody who could take his place.

Some early cock-ups were probably linked to lack of people. The United States might not have lost its seats on two influential United Nations committees (human rights and drug control) if it had had a permanent UN ambassador in place.

There are more problems on the way. The budget is the engine that drives the Washington bureaucracy. Only three departments have appointed chief financial officers. So they may be late in submitting their budgets to the Office of Management and Budget, and the OMB, in turn, may be late in compiling the budget.

The appointments process has got more troublesome with each new administration. John Kennedy had his cabinet and sub-cabinet in place by April 1961; Bill Clinton had to wait until October. Now that Mr Bush will have to wait a year to complete his administration, the system is a farce. "Disastrous", "a national disgrace", "on the verge of collapse" are some of the more temperate phrases that academic commentators have used.

What went wrong?

It is hard to blame Mr Bush for much of this; he is generally deemed to have done most things by the book. The underlying, institutional reasons begin with the multiplication of political appointees. In 1961, Kennedy had just 118 senior appointments to fill; today the number is closer to 300.

A second reason is the absurd multiplication of bureaucratic tests. Every new scandal means another set of hoops for the hapless nominees to jump through: America now has to protect itself not just from the communist threat but also from the illegal nanny threat. Nominees must subject themselves to background checks by the White House Office of Presidential Personnel, by the Office of the Counsel to the President, by the FBI and by the Office of Government Ethics. They must answer more than 230 questions, and list all the foreign trips they have taken in the past 15 years, along with the purpose of the visit, and all traffic fines they have paid over $150. For some reason known only to the gigantic vetting industry, the replies also have to be filled out by typewriter.

The change in power in the Senate will not help

A third reason is the Senate's abuse of its "advice and consent" power. That power was supposed to allow a Senate majority—51 senators—to check the more controversial nominees. But in recent years it has become an excuse for individual senators to impose "holds" on potential nominees to advance their own causes or simply to exercise personal spite. Jesse Helms is holding no fewer than four treasury nominees hostage until he is allowed to rewrite last year's Africa-Caribbean free-trade bill, in order to protect textile interests in his native North Carolina. Hillary Clinton, who is holding up a consumer-products safety commissioner, may become the Jesse Helms of her party.

The change in power in the Senate, thanks to Jim Jeffords's defection from the Republicans, will not help. If Mr Bush is lucky, the handover of power will delay the nomination process by a few weeks. But it could be far worse than this if Democratic senators drag their feet over Bush nominees—as the Republicans did over Mr Clinton's people.

Many senior Democrats have their minds not on the smooth running of the current presidency but on their own presidential ambitions in 2004. A bumper crop of senators are gearing up for tough election battles in 2002. And the ever diligent Senate goes into recess from early October until January. The idea that the Bush administration will be complete by next March may yet be too optimistic.

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Lexington

Tiger, Tiger, burning bright

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In his attitude to race, Tiger Woods is as precocious as in his game

FOR once the over-used claim that a sportsman is “unique” may make sense. Tiger Woods can hit a golf ball with greater consistency than anyone else in the world. He is the only golfer ever to hold all four top professional titles in the game at once. The only question is whether his dominance will be confirmed this weekend with victory at the US Open in Tulsa, where he could win an unprecedented fifth major title in a row, or with some other milestone in the near future. He has won $25m in prizes and earned far more from sponsorship and endorsements. He may become sport’s first billionaire.

All this Mr Woods will acknowledge. His beaming delight in his victories and his dedication to honing his talent speak of a man who is not just sure of his strengths but fiercely proud of his achievements. But there is one aspect of himself Mr Woods does not acknowledge as special. That is his race.

In a game long played in clubs to which no Jew or black man was admitted, and where many are still not particularly welcoming, Mr Woods, with his dark skin and black hair (except when he bleaches it for a lark), might have been expected to revel in his conquest of the inner sanctums. But he chooses not to. He acknowledges the mixture of black, white, Native American, Chinese and Thai in his parentage, but claims no special privilege for it. Far from seeing himself as a lone black face in a sea of white ones, as Arthur Ashe used to be on a tennis court (and as the Williams sisters still imagine they are), Mr Woods sees himself as just another Californian hybrid.

Demographically, his attitude seems obvious. Why bother to make a fuss about not being white if you come from a state where non-Latino whites are now a minority? Why preach the benefits of multiculturalism when the races you grew up with are becoming ever less distinct? More than 40% of third-generation Asian-Americans marry people of different ethnic backgrounds. Among Latinos, who are racially even more disparate than Asians, almost two-thirds marry non-Latinos. Among African-Americans intermarriage rates are lower, but nevertheless higher than ever before and climbing. The census last year, for the first time, allowed people to register their race as a combination. Across the country 7m people, mostly young ones, took advantage of this opportunity.

So Mr Woods is no oddity in terms of demographics. But he is in terms of politics—particularly black politics. Black leaders who took a dim view of the proliferation of ethnic categories on the census form, believing they would diffuse the power of minorities, patently feel uncomfortable with this new role-model. Mr Woods was chided by black leaders when he described himself as “cablinasian”—a little bit of all his forebears—in an interview soon after the start of his professional career. Instead, his critics insisted, he should call himself black, since his blackness would define the obstacles he would face.

White men can’t jump, throw, run...

Even when set alongside Colin Powell, the national black politician who plays the race card least, Mr Woods stands out. He does not play the card at all; indeed, he seems to deny that it exists. The fact that he is a sportsman probably only increases the radicalism of his non-position. The idea of the black athlete struggling against oppression to secure his or her dream is part of black mythology: Jackie Robinson making the major leagues, Jesse Owens humiliating Hitler, black-power salutes at the 1968 Olympics. And rightly so: in those days, black Americans were clearly discriminated against. But the idea that there is a specific racial barrier in modern American sport, as opposed to barriers of poverty and background that apply to all races, looks increasingly hard to sustain. People of colour are well represented in every big American sport—except golf, which only makes Mr Woods an even more awkward figure.

Ironically, a man who does not want to be seen as either black or a politician is a symbol for a series of huge questions nagging away at black America. Nobody denies that blacks have a uniquely awful history among Americans (though Native Americans come close), nor that they contend with more consistent racial prejudice than any other group. But with the black middle class growing bigger by the day, are racial-preference programmes still necessary? Should blacks really think of themselves as a distinct group in need of a “black leadership”? Above all, even if blacks want to keep that distinction, how do they relate to other groups who increasingly seem not to share it?

Asian-Americans never really went down the route of group advancement in the first place (and have, in general, prospered mightily). In the 1970s Mexican-American activists formed the Chicano movement, which was loosely based on the black model; but its rhetoric of fighting for rights as a victimised group has faded in the face of diverse Latino success in business and culture. That is not without its drawbacks. In the recent mayoral election in Los Angeles, blacks, by voting as a traditional block (and voting in large numbers), helped deliver victory to James Hahn; black districts will surely benefit. By contrast, Latinos, proportionately, failed to turn out for Antonio Villaraigosa. They seem to think their future depends more on the city’s economy than either the race of its mayor or their own electoral clout.

The idea of “post-racial politics” may be just a pipedream; but that does not mean that politics will not move in that direction. Mr Woods’s quiet presumption that he should be celebrated for his golf alone is the view of someone who is already on the other side of whatever obstacle there was. By the time he is 46, the age at which Jack Nicklaus won his 20th major, whites will make up less than 40% of Californians, and nobody will raise the question of his family background, so unremarkable will it seem by then. Mr Woods has simply arrived in the future ahead of everyone else. As usual.

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Chicago's schools

Drawn upwards

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Magnet schools seem to work—but only for those in them

WHEN the doors opened at Chicago's Northside College Prep High School in the autumn of 1999, it was the first new public high school built in the city in 20 years. The architecture in the $45m building is inspiring; the corridors glisten. There are computers in every classroom and no bells or buzzers. Music marks the end of every class. And every student at Northside College Prep is above average. Really.

Northside is the flagship for Mayor Richard Daley's plan to keep talented students in the public schools and retain middle-class families in the city. Beginning in 1997, Chicago opened six new "magnet" high schools and a magnet military academy. The system now has ten academically selective high schools and a performing-arts magnet academy. Only the most talented students need apply. Northside accepted the 240 students who scored best on the entrance exam from nearly 5,000 applicants; some 30% of the students accepted were lured away from private schools. So was its headmaster.

Magnet schools certainly help keep the brightest students in the system. In 1995, 27% of the top students quit the public system after eighth grade; in 2000, only 15% did. "It's pretty clear that they're keeping stronger kids," says John Easton, deputy director of the Consortium on Chicago School Research. The magnets have also pulled back white middle-class children. Although only one in ten of the students in Chicago's public schools is white, the magnet high schools look more like the city as a whole: 24% white, 43% black, 20% Latino and 13% Asian.

Still, Mr Daley has more school headaches than at any point since he took control of the system in 1995. In May, the president of Chicago's school board, Gery Chico, resigned. Now the chief executive of the Chicago Public Schools, Paul Vallas, has gone too. As with Mr Chico, the mayor apparently applied pressure. ("The writing was on the wall—all over the wall. In fact, it was like graffiti," Mr Vallas admitted.)

Mr Vallas has much to show for his six years in office: better test scores, improved attendance and graduation rates, stable finances, and nearly $3 billion spent building new schools and repairing old ones. But after six years of steady gains, test scores have gone flat. A particular disappointment are reading scores in the third grade (nine- and ten-year-olds), which showed no improvement, even though this year's class was the first to have had more intensive instruction since kindergarten. Two in five students still drop out before finishing high school. Middle-class families whose children do not get into a magnet school are still likely to prefer the suburbs or a private school over their local public school. As the *Chicago Tribune* concludes, "While Chicago schools are better, they are not by any definition good."

Mayor Daley has chosen Michael Scott, the president of his parks board, to be the new school-board president, a part-time and unpaid position. He has not selected a new CEO. The candidate thought to be Mr Daley's top choice, Mary Dempsey, the library commissioner, has expressed reservations that the job will "consume her".

Meanwhile, the labour peace that has made school reform possible has grown tenuous. The Chicago Teachers' Union has elected a new president, Deborah Lynch-Walsh, who promises a less cosy relationship with the mayor; he has publicly endorsed her opponent. Ms Lynch-Walsh has criticised policies that punish teachers in failing schools. She prefers the familiar union standbys: more spending and smaller classes. Before 1995, Chicago teachers went on strike nine times in two decades, leaving the system in perpetual disarray.

Even the shimmering magnet academies draw criticism. Magnets, like all forms of meritocratic education, "cream" the best teachers and students from the rest of the system. Only one in ten of Chicago's high-school students are in magnets; the rest are stuck in schools that are improving slowly, if at all. Predictably, teachers are asking whether the resources lavished on the system's best students might be

better spent on the more needy. On the other hand, it was lack of excellence and terror of experimentation that got Chicago's school system into its mess in the first place.

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School life

No time for play

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And that man over there is a lawyer

IF THE children spilling on to America's streets this month for their summer holidays seem to take extra delight in their freedom, the reason is not hard to find. At one school after another across the country, recess ("break" to Brits), the 15-minute periods of "non-directed activity" ("play" to non-child-psychologists) have disappeared. Once, the tedious mornings and afternoons were gloriously broken by the bell and the stampede outside. No more.

The perils of being non-directed

The trend began in the mid-1980s, and has been all downhill since. Atlanta seems to be the only place to eliminate recess in a whole school district; but individual schools have done so in Michigan, Wisconsin, New Jersey, Florida, California, Kentucky and Maine, to name only a few mirthless places.

Some parents are not taking this lightly. The American Association for the Child's Right to Play, an organisation based at Hofstra University in New York, gets around 300 furious calls a day. In May, more than 1,000 people, many of them serious academics, showed up at an association conference ("The Child's Right to Play: a Global Approach") to grapple with such topics as "The moral and ethical dimensions of controlling children's play", and "The role of the expert witness in playground litigation". More on that later.

The association's president, Rhonda Clements, who is also a professor of education at Hofstra, thinks recess may always have been a bit controversial. An 1885 memo from a Michigan school superintendent expresses concern over children being improperly clad against the cold, "maimed for life" by boisterous older children, mauled by bullies and giving vent to foul language.

None of these concerns has gone away. Supervision, once done by principals under the premise that this would allow them to see the children in their truest light, has often been relegated to part-time assistants. As a result, says Anthony Pellegrini, a pro-recess professor at the University of Minnesota, crucial but subtle distinctions are missed between, for example, whether boys are pounding each other in fun or sport (good) or trying to kill each other (bad).

There's less time for break, too. With more standardised tests and increasingly packed curriculums, anything that sounds like fun gets pushed aside. But, this being America, litigation may be the main culprit. In a survey of 523 elementary schools by the National Association of Elementary School Principals, more than one-third said that lawsuits and problems with insurance had forced them either to modify or drop recess. Some schools have stripped play areas of any equipment, to pre-empt lawsuits from people who fall off swings when they break in after hours.

For fans of play, however, all is not lost. Even outside Hofstra University, a backlash has started. Last year, Virginia became the first state to make recess a daily requirement. Texas, which has many no-recess schools, is re-evaluating its hands-off position. Philadelphia could soon put a pro-recess initiative on the ballot. Florida may do likewise in a few years. Given that state's crucial role in national elections, and the delicate party balance of its population, a clever, school-reform-minded politician may want to take up the cause. Children will be grateful, and will no doubt make their feelings known in the strongest possible manner to the voters in their family.

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The great beret affair

Badge of honour

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Well, hardly

ONE problem with political manoeuvring in Washington, DC, is that it usually ends up squashing somebody. There have been few better examples of Beltway bluster than the great beret controversy—the storm following the revelation that American soldiers would supposedly have to don Chinese headgear. Now the tiny town of Cabot, in the Arkansas Delta, has been hit by one of the gusts.

For more than a century, the Bancroft Cap Company, one of Cabot's main employers, has been making hats. For the past 20 years, it has made most of the army's berets, including the distinctive black ones for the elite corps of Army Rangers. Last autumn, the Pentagon decided that as of this Thursday, June 14th, the army's 226th birthday, all its soldiers should wear black berets like the Rangers. Bancroft was awarded an $8m contract to make 1.3m black berets—roughly a quarter of the total order. Barry Goldman, the third generation of his family to run Bancroft, duly hired more employees and bought new equipment. Talk bubbled about a second factory being opened—a big thing in the Delta.

Then the complications began. Bancroft said it would have trouble meeting the June deadline; that helped spur the Pentagon to waive a long-standing rule on producing uniforms in the United States. It ordered berets from a Canadian firm and two British ones, one of which, Kangol, uses a factory in China. When this emerged in February, it provoked howls of fury from politicians. And after the China spy-plane incident, the Chinese part of the foreign contracts was ditched in May.

Meanwhile, a separate row broke out, because many Army Rangers objected to the idea of lesser types being allowed to wear their black berets. Former Rangers marched on the Capitol to protest and circulated petitions on the Internet.

At first neither dispute had any effect on Bancroft: it added staff and churned out the berets. Then, in May, the Pentagon's Defence Contract Management Agency announced an inquiry into allegations that the company was violating the (aptly-named) Berry amendment, which has prohibited the use of foreign materials in products bought by the Department of Defence for more than 50 years. Bancroft immediately had to halt beret production, and 50 people were temporarily laid off.

Nobody at Bancroft disputes the charge. The company has never made a secret of the fact that 10% of its wool blend comes from overseas, and that the leather straps on the beret are made in Pakistan. What amazes Mr Goldman is that the Pentagon, after years of accepting this arrangement, should suddenly seem so shocked by it—even more bizarrely when, at the same time, it has just started getting entire berets made overseas.

The Cabot city council turned to their congressman, Marion Berry, a conservative Democrat with no connection to the eponymous amendment. After a bit of congressional sleuthing, Mr Berry claims that the investigation has nothing to do with the berets' origin and everything to do with their colour and with Ranger pique. He says that three Republican congressmen with strong connections to the Rangers (Mr Berry will not name them) pushed the Pentagon into the investigation, hoping to dissuade the army from black berets. The army has not budged, even though production delays mean that only 336,000 troops—a third of the total—had received their black berets by its birthday this week.

Mr Berry, who has kicked up something of a public fuss about this, hopes that the office of Donald Rumsfeld, the secretary of defence, will produce a waiver to allow Bancroft to resume beret production. As *The Economist* went to press, Bancroft was still waiting. Without a waiver, the company may well go out of business, leaving 165 people unemployed and the black berets to be made by non-patriots overseas. There are surely better ways to celebrate the army's birthday.

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Corruption in Latin America

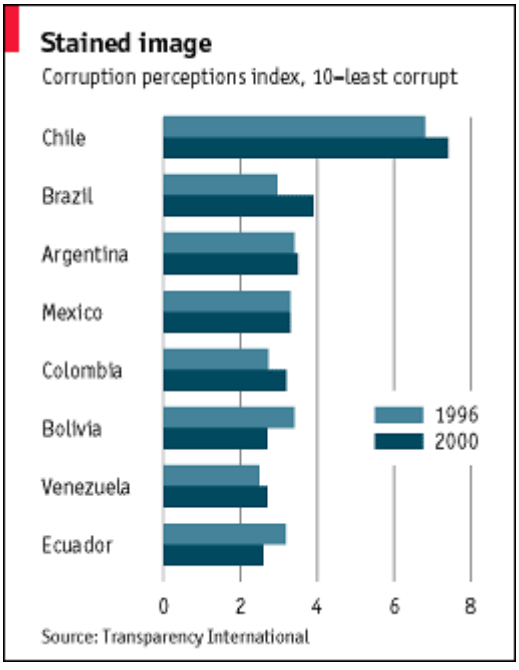
Wanted—a crusade to purify public life

Jun 14th 2001 | BRASILIA AND MEXICO CITY
From The Economist print edition

A rash of scandals is testimony to greater scrutiny as much as more widespread sleaze. But there are many more things governments could do to clean up

ARGENTINA'S former president, Carlos Menem, is under house arrest on suspicion of involvement in an arms-trading scandal. Paraguay's president, Luis Gonzalez Macchi, who was recently discovered to be driving a stolen BMW car, faces calls for his impeachment over fraud allegations, as does Brazil's Senate president, Jader Barbalho. In Peru, more than 60 people—among them politicians, judges, generals and businessmen—have been detained, caught in the web of corruption spun by the regime of Alberto Fujimori, who was ousted as president last year. In Colombia the national auditor's office reported this week that corrupt officials creamed off $27m last year from the education budget. In Mexico President Vicente Fox has launched a plethora of initiatives to crack down on endemic corruption.

Mr Menem has not been charged, and denies all wrongdoing. But the arrest of a former president until recently seen in some quarters as a symbol of modernisation has shaken Argentines. And across Latin America opinion polls reveal a belief that corruption is flourishing as never before. In a region where poverty and inequality remain disappointingly widespread, perhaps nothing is more corrosive of public trust in democracy than the belief that the politicians impose austerity on the many while lining their own pockets, and those of their fat-cat friends in an often monopolistic private sector. But belief may be outstripping reality. Corruption is notoriously hard to measure. However, surveys of how prevalent businessmen and others believe it to be, carried out by Transparency International, a non-governmental organisation, suggest that though some Latin American countries are becoming more corrupt, others are improving (see chart).



Certainly, privatisations have too often been tainted by corruption, and contracts padded, and bribery and influence-peddling remain common. The drugs trade and the need to finance political campaigns have both played a role in spreading corruption. But a sense of perspective is needed. Democracy, and a smaller role for the state in the economy, reduce the opportunities for sleaze. The biggest corruption scandal in Latin America was probably in Venezuela in the 1980s, when a government decision to adopt multiple exchange rates saw $11 billion in hard-currency reserves vanish. Under the dictatorship of General Alfredo Stroessner in Paraguay, corruption was the rule rather than the exception. Its critics would say the same of the rule of Mexico's Institutional Revolutionary Party (PRI), ended by Mr Fox's election victory last year.

Indeed, the current crop of corruption scandals may merely be a sign that wrongdoing is more likely to be exposed. In Brazil, "there has never been as much transparency as now, and there has never been a government so willing to avoid covering things up as now. Never was society so demanding as now, nor the media as active," President Fernando Henrique Cardoso told *The Economist* this week.

Many countries have enacted reforms that should inhibit corruption. Brazil, for example, now has compulsory competitive tendering for government purchases, and a requirement that local and national

governments produce detailed accounts.

But the effectiveness of such laws is too often undermined by judicial failings. “The big gangsters have lawyers and use the justice system to block their cases from advancing,” says Mr Cardoso. Attempts to reform Brazil’s civil and penal code have got nowhere. In Argentina, Mexico or Mr Fujimori’s Peru, judges and prosecutors have been susceptible to political pressure. In Nicaragua, whose media are unusually free and feisty for a small Central American country, tame judges have helped corruption to persist. But in some countries there are signs that the judiciary is becoming more independent.

Governments could have done much more to clean up public life. At the first Summit of the Americas in 1994, the continent’s leaders drew up a grand plan against corruption. In 1996 they agreed on an Inter-American Convention Against Corruption. But the good intentions expressed in both documents have largely remained just that. On June 4th, at the Organisation of American States’ annual meeting in Costa Rica, the governments at last agreed to create a vague “follow-up mechanism” to monitor each other’s progress on implementing the convention.

The World Bank has faced resistance in some countries to its offers to pass on know-how to combat corruption. But not everywhere: in Colombia, the Bank has begun a confidential survey of public officials and government suppliers, to try to gauge how much corruption exists and how it is carried out. In Brazil Marta Suplicy, the new mayor of Sao Paulo, who is from the moderate wing of the opposition Workers’ Party, has invited the Bank to help her stamp out the countless frauds that have added to the problems of South America’s largest city.

In the end, says Miguel Schloss, Transparency International’s director for Latin America, there will be successful action against corruption only if the process is depoliticised. In Chile, for instance, the organisation’s local branch assembled a cross-party group to report on the government’s compliance with the Inter-American Convention Against Corruption. No one accused the group of political bias, says Mr Schloss.

But in many countries the fight against corruption remains a partisan, rather than civic, cause. In Brazil, the opposition is seeking a wide-ranging congressional inquiry into various corruption claims against figures in the governing coalition. That might do some good if it were conducted responsibly. But Mr Cardoso seems to have a point when he argues that it is motivated less by a genuine desire for a thorough investigation than by a wish to throw as much mud at him as possible in the year before a presidential election.

Yet corruption has tended to flourish where political opposition is weak, as in Mexico under the PRI, in Colombia, or in Venezuela’s two-party oligarchy, turfed out by Hugo Chavez in 1999. That makes Mr Chavez’s concentration of power in his own hands look ominous. So is a power-sharing pact in Nicaragua between the ruling Liberals and opposition Sandinists.

A vigilant (if not partisan) opposition, inquisitive media, a stirred up citizenry, independent judges, tighter rules and more open government: all are needed if Latin America is to clean up its democracy.

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Canada

Vive the difference

Jun 14th 2001 | MONTREAL
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C'est officiel: French is not under threat

LANGUAGE, more than anything else, defines Quebec. The province, after all, is the only significant French-speaking region not just in Canada but in North America. For three decades, defensiveness has defined the provincial government's approach to language. And the best way to defend French is to stop people speaking anything else—especially English.

This has led to legislation that many Canadians consider draconian. Immigrants to the province, for instance, are not allowed to send their children to state-run English schools. Shopkeepers must make French clearly predominant on all their signs, even in places where most of their customers speak another language.

But now, an "estates-general" set up by the Quebec government has come to a surprising conclusion: French, it turns out, is not under threat in the province. The commission, led by Gérald Larose, a respected, priest-like former union leader who may soon join the Parti Québécois (PQ) government, does not recommend any loosening of the language laws. But neither, it says, is there any need to stiffen them, as PQ hardliners argue. And Mr Larose urges the scrapping of the Orwellian bureaucracy created to deal with language issues, which is notorious for measuring shop signs and insisting that coasters for imported beer be made bilingual.

The long-term danger, the commission suggests in its preliminary report, is not such linguistic trivia, but the poor quality of French spoken in the province. It wants better teaching, and also, surprisingly, of English. The logic: bilingualism could give Quebec a real competitive advantage. And the commission recognises that, if English still posed a threat, this would not come from the bilingual, and much-reduced, English-speaking minority in the province.

Such proposals have won reluctant praise from many federalists. Most of them, including the provincial Liberals who boycotted the commission, had seen the estates-general as an elaborate propaganda device by a secessionist government eager for fuel to power its next election or sovereignty referendum. Conversely, the PQ faithful feel let down, especially by Mr Larose's relaxed tone. "Some people would say I'm smoking some really good stuff," he said. But he has proposed one measure to the PQ's liking: that Quebec should institute its own citizenship. However symbolic, that would increase Quebec's psychological separation from the rest of Canada.

The estates-general may have upset the plans of Bernard Landry, who took over as provincial premier in March after his predecessor had resigned. Mr Landry was widely expected to call an election this autumn to try to win a mandate of his own. Though he has refused to comment until the estates-general issues its final conclusions in September, the premier has implicitly recognised that it is unlikely to help the PQ's cause. On the day the preliminary report was released, he said that he would not call an election until next year.

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Colombia's drug war

Spraying protest

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A riot by coca farmers poses a dilemma for the government

THE American-backed offensive against drug crops, launched last December under the rubric of "Plan Colombia", involves a carrot-and-stick approach. The carrot is money for alternative economic activities. The stick is widespread aerial eradication of coca fields. Now the government of President Andres Pastrana is facing pressure to halt the spraying.

This month police crop-dusters have been spraying weedkiller in Norte de Santander, over about 7,000 hectares (17,300 acres) of coca. But last weekend several thousand coca farmers and labourers descended from their hillside fields and took over Tibu, a town near Colombia's border with Venezuela. They looted local businesses, and set fire to tanks of weedkiller stored at the town's airstrip. The farmers are refusing to leave the town until the government stops spraying.

This was the first big protest against Plan Colombia's spraying campaign, but it came as American officials were already casting doubt on the commitment of Mr Pastrana's government to forced eradication. Between December and mid-February, about 25,000 hectares of coca were sprayed in Putumayo, home to around half of the total crop (estimated at 136,000 hectares by the United States). The government then halted spraying there and instead employed 29,000 coca farmers to undertake the manual eradication of their plants. It has ordered no spraying in neighbouring Caqueta, a stronghold of the FARC guerrillas, with whom it is holding desultory peace talks. But in February and March it did spray 5,600 hectares of coca in the south of Bolivar department.

The FARC is bitterly opposed to aerial spraying. But so, too, are the right-wing paramilitaries of the United Self-Defence Forces of Colombia (AUC). Both groups make money from drugs. Gonzalo de Francisco, the government official in charge of Plan Colombia, cites police reports that the AUC, which controls much of Norte de Santander, was behind the taking of Tibu. He insists that Plan Colombia will go ahead in the area, but that manual eradication is a possibility. Officials were due to visit Tibu this week to discuss alternative development.

The ferocity of the protests recalls those in 1996, when seven people were killed as 60,000 coca farmers and labourers clashed with the security forces in Putumayo, Caqueta and Guaviare departments. Those protests were said to have been organised by the FARC.

The new revolt poses a dilemma for Mr Pastrana. He wants to keep American support—and he wants to weaken both the FARC and the AUC by cutting their drug income. On the other hand, for many farmers coca is the only reliable source of income. Forced eradication is unpopular, and there is an election next year.

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Education in Chile

Back to school

Jun 14th 2001 | SANTIAGO
From The Economist print edition

Big efforts have been made to improve Chile's education. Not big enough

THE centre-left governments that have run Chile for the past decade are proud of their commitment to education. Spending on education has doubled in real terms over the 1990s. Reforms have been carried out to try to ensure that poorer Chileans get better schooling. But businesses say they still find it hard to get well-educated workers. And there are signs that poor educational standards may be starting to hold back economic growth.

A recent study of 49 countries by the International Institute for Management Development, a Swiss business school, seems to bear this out. Among the nations studied, Chileans worked the longest hours, but their productivity was among the lowest, though still higher than in most other Latin American countries. Another study, this one by the OECD, found that four Chileans out of five did not fully understand even what they read in their own language. No wonder technology firms complain about the difficulty of hiring staff who can read manuals in English.

In part, these shortcomings may stem from the past: two-fifths of the labour force did not finish secondary school. Today over 80% of children complete secondary education. President Ricardo Lagos, a former education minister, wants to increase that to almost 100% by the end of his term in 2006. He has asked the World Bank for a loan to help adults to return to school to complete their studies.

Chile devotes 7% of its GDP to education, but almost half of that is spent by parents, either on higher education or on private schooling for the 10% of children who do not go to state schools. The previous government tried to make education more equal. Its education reform aims to extend the school day, by abolishing the two-shift system on which half of Chile's state schools still operate. It also seeks to modernise the syllabus and improve teacher training.

Officials reject criticism that the results have been disappointing. They point out that children educated wholly under the new system have yet to graduate. But critics say that the reforms have failed to improve the quality of schooling.

Chile allows private companies to operate state-financed schools. It has also tried to create competition: parents can choose which schools their children attend. State schools get a monthly grant, which varies with the number of pupils enrolled and their attendance record. But in practice parental choice is limited because poorer parents lack information, and cannot afford the bus fare to more distant schools in better-off areas. Neither can bad teachers or heads be easily sacked.

Some educationalists blame lack of resources, rather than inefficiency, for poor school results. "It's easy for business leaders to complain. They send their children to private schools that charge $300 a month, while state primary schools receive a tenth of that amount," argues Jose Joaquin Brunner, of Fundacion Chile, a quasi-governmental technology institute.

One way to close that gap would be to attract more private donations to state schools. For example, Colegio San Joaquin, a state-financed school run by a private foundation in a poor area of Santiago, the capital, has a well-stocked library, and modern science and computer facilities, mostly paid for by private sponsors.

The government wants to expand the number of technical schools, some of which offer apprenticeships. But many businesses are loth to offer places to apprentices, according to Jose Weinstein, the deputy minister of education. That is partly because they fear accidents, and thus higher insurance premiums. The Association of Manufacturers, which runs five technical schools, solved the problem by asking parents to contribute $30 a year to buy their children accident insurance. Businesses could also make fuller use of tax credits for workplace training.

Along with a plan to reform Chile's health system announced by Mr Lagos last month, higher educational standards are central to the government's hope of achieving its promise of "growth with equity". But a decade of educational reform suggests that, though Chile is ahead of most of its neighbours in such aspirations, it is still far behind the rich world.

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Japan

The day of the governors

Jun 14th 2001 | CHIBA CITY
From The Economist print edition

Once the pliant tools of Tokyo, the governors of Japan's 47 prefectures are starting to assert themselves

AN UNWANTED dam in Nagano. A controversial tax on plastic bags in Tokyo. A fight in Chiba to save precious wetlands from the bulldozers. The stuff of Japanese local politics might seem low-grade fare beside the larger drama now unfolding on the national stage. Yet amid the talk of a revolution in Nagatacho, Tokyo's political district, it is important not to forget the many minor acts of rebellion that went before it. Junichiro Koizumi, Japan's reformist prime minister, came to power in April on a wave that began, in a thousand small ways, in the regions.

The most eye-catching change has been among Japan's local political leaders, until recently as grey and as dull as their counterparts in Tokyo. In October, the conservative voters of Nagano, a rural prefecture, chose as their new governor Yasuo Tanaka, a chubby playboy novelist with a fondness for tight leather suits. In March, the people of Chiba, another conservative bastion, elected as their governor Akiko Domoto, a former journalist who began her campaign with no party backing and a support group of just 60 people. Shintaro Ishihara, the novelist and media celebrity who governs Tokyo, has brought life and colour—and a worrying whiff of nationalism—to the capital's politics.

It is not just their style that sets these politicians apart. Traditionally, Japan's 47 prefectural governors have enjoyed intimate ties with the old home-affairs ministry (now part of the leviathan Ministry of Public Management, Home Affairs, Posts and Telecoms), a throwback to the pre-war system under which the ministry appointed Japan's regional bosses directly.

Even now, despite more than 50 years of democratic governors' elections, over half of the governors are still ex-bureaucrats. Thanks to the nodal position of the prefectures, sitting as they do between the centre and Japan's 3,200 municipal governments, these ties have helped to preserve in modern Japan some of the features of pre-war society: uniform, centrally-determined policies and docile obedience in carrying them out. But Japan's economic woes have dragged the reputation for economic competence of the ruling Liberal Democratic Party (LDP) through the mud, and all the old frustrations with top-down rule—which last surfaced in the 1960s—have come bubbling to the surface again.

The evidence is everywhere. In Nagano, Mr Tanaka won with the support of citizens' groups that opposed a dam the construction ministry wanted built against the wishes of local residents. Akio Fukuda won in Tochigi on a similar platform. Masayasu Kitagawa, the governor of Mie prefecture and a pioneer of the new confrontational style, won celebrity last year by opposing the construction of a nuclear power plant. The government and the utility company, Chubu Electric, had been trying to build this plant, against local opposition, for 37 years.

In Chiba, Miss Domoto wants to cancel a land-reclamation project that Tokyo's bureaucrats have been pushing for nearly 30 years. The project, which would create land for new factories, has long since stopped making sense, says Miss Domoto: thanks to the weak economy, Chiba has plenty of empty factory space already.

Calls for referendums are being heard all over Japan, on all manner of issues from rubbish dumps to airports. Local politicians have begun to realise that there are votes in championing them. After a referendum in Tokushima in which the locals voted against a new dam, the mayor, a construction-ministry old boy, abandoned his support for the project. Instead, he threw in his lot with the anti-dam lobby and was duly re-elected.

Along with opposition to the centre comes a more humble approach to government. Here and there, the usual arbitrary rule is giving way to more enlightened attitudes. In Mie Mr Kitagawa has introduced a system to evaluate the cost- effectiveness of major items in the prefectural budget. Everything is disclosed, for voters to see, on the Internet. In six years, says Mr Kitagawa, 800 of the prefecture's 3,300 budget items have disappeared. Mr Tanaka's administration in Nagano has become so transparent that he even sits behind glass walls, through which voters can see their governor at work.

Clearly, Mr Koizumi owes a debt to the regions. With his sharp suits and his flair for political theatre, his style borrows heavily from the most popular of Japan's new governors. His reforms, meanwhile, mirror their confrontational politics. A plan to review the huge road budget pits Mr Koizumi against his own party's strong construction tribe. A call to reduce local-government subsidies takes on the bureaucrats of the old home-affairs ministry. "Reform with no sacred cows" sounds a suitably revolutionary note for a man who himself came to power—against the wishes of the antique leadership of the LDP in Tokyo—thanks to a revolt among the party's local chapters.

Yet it should be remembered that, besides championing this revolution, Mr Koizumi must also find time to lead his party. Miss Domoto, Mr Tanaka, Mr Ishihara and the other unruly governors owe their success to their independence. No party affiliation binds them to the establishment: they attack it from outside. Superficially, Mr Koizumi resembles them. Yet if his reform drive were to falter, the voters might come to see him not as Japan's salvation, but as just another part of its problem.

If that happened, his support could quickly melt away. In 1868, samurai from the two remote southern domains of Satsuma and Choshu seized the imperial palace in Kyoto, declared the restoration of the Meiji emperor and brought to a sudden end two-and-a-half centuries of rule by the Tokugawa shogunate. Mr Koizumi will need to watch his back.

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Caste in India

Still untouchable

Jun 14th 2001 | DELHI
From The Economist print edition

Should India's caste system be equated with racism?

"CASTE is worthless and so is its name," proclaimed Guru Nanak, the founder of the Sikh religion. Yet in the village of Sidhwan Khurd in Punjab, one of India's richest states, there are two *gurdwaras* (Sikh houses of worship), a scruffy one for the village's "scheduled castes", the official name for people who used to be called untouchables, and a spiffier one for other Sikhs. India's 160m Dalits—as members of its scheduled castes call themselves these days—suffer worse privations than segregation at prayer. But nothing shows better than Sidhwan Khurd's two *gurdwaras* how stubborn is the stigma of untouchability, 500 years after the Sikhs abolished it and 50 years after the Indian state did so.

Panos

Children of God

That is why Dalit activists want their plight to be on the agenda of a forthcoming UN conference on racism, to be held in South Africa in August. Their demand has triggered a debate in India about the nature of caste discrimination and whether it is a subject fit for discussion by other countries. The government is reluctant. "Race and caste are distinct," says Soli Sorabjee, India's attorney-general. Although India has been a vigorous campaigner against apartheid, it does not much like the idea of having outsiders poking around its own systems of stratification.

India does not practise anything like official apartheid. On the contrary, a fifth of the seats in Parliament are reserved for members of scheduled castes and tribes. They and other lower castes have places at educational institutions and jobs in government ear-marked for them. Some states have powerful political parties based on alliances among lower castes. India's president, K.R. Narayanan, is a Dalit.

Yet quotas and job-preferment have not brought equality, dignity or even safety to India's lowest castes. Dalits are barely represented among the grandees of business, one reason why some demand reservations for jobs in the private sector. They are over-represented, however, in the ranks of landless agricultural labourers and illiterates. Such humiliations as the "two-tumbler system" (separate glasses for Dalits and non-Dalits) persist in some places. In villages, the stigma can lead not just to segregation but to violence. Recorded crimes and atrocities against scheduled castes averaged 26,000 a year between 1997 and 1999; in 1998 that included 570 murders and 931 rapes.

Dalit activists see no reason why these injustices should not be discussed at the UN conference, which is to discuss not only racism but "racial discrimination, xenophobia and related intolerance". Just like racism, discrimination against Dalits is "based on descent", argues Martin Macwan, convenor of the National Campaign on Dalit Human Rights. Nor is it restricted to India: Mr Macwan says that people of Dalit stock are discriminated against in Pakistan, Bangladesh and Nepal as well.

Mr Sorabjee does not deny that "caste discrimination is prevalent in India." But the government has a hard time admitting that it is an Indian variation of a worldwide phenomenon, worthy of international scrutiny. Even Dalits themselves are not free of prejudice. In the matrimonial section of a website for Dalits, advertisers boast of prospective spouses' "fair complexions".

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East Timor

Ready to fight

Jun 14th 2001 | AILEU
From The Economist print edition

Former guerrillas turn regular

Get article background

AP

Doing it by the book

AS TALKS on reconciliation between its independence heroes and their pro-Indonesia militia foes get nowhere, East Timor has given up the idea of turning itself into an Asian Costa Rica, with only a police force and no standing army. Instead, in the hill town of Aileu, the first recruits of the new East Timor Defence Force are now going through their paces. Come independence, which is expected later this year or early in 2002, this force of ex-guerrillas will have to defend the sensitive border with West Timor, where the militiamen are waiting just over the hill.

The first batch started training in February, most of them drawn from East Timor's old resistance army, Falintil. They still carry that name on their uniforms for old time's sake, but these days they are wearing full military dress. Taur Matan Ruak, Falintil's former chief, has been appointed a brigadier-general and is technically in command, although he has Australian and American advisers. The course, including five weeks' basic training and instruction in human rights, is run by the Portuguese army.

Strangely, some of the nearly 700 recruits are former Timorese soldiers who once served in the Indonesian army. There is even one from the Kopassus special forces and one from the Kostrad strategic reserve, two units widely associated with atrocities in East Timor and elsewhere. Some of the Timorese soldiers who joined Indonesia's army got a terrible name for barbarity against their own people, but others leaked useful inside information to the guerrillas. Many voted for independence in the 1999 referendum.

Their barracks are simple and the pay next to nothing, but there is no doubting their commitment. The average age is 42, two years older than Major Jose Afonso, the Portuguese chief trainer. The oldest is 56. The men know how to kill and have their own style of discipline, but they are not used to the formalities and rigours of a modern army. They did not have ranks in the jungles, where many of them spent the entire 24 years of occupation, just "commanders" and "troops", and now they are having to learn correct safety procedures for their weapons.

Ultimately, the force will be 3,000 strong: 1,500 regulars and 1,500 reserves. The current recruits include 250 officer candidates, selected by the Portuguese trainers. Aileu was chosen as a base because Falintil was founded there in the mid-1970s and encamped there before the 1999 vote. Although wrecked by the militias like the rest of East Timor, for Falintil it is a sanctuary.

The UN advisers putting the army together say they have deliberately structured it as a defensive force that will be able to see off militia incursions. There have been a series of these, in some of which UN peacekeepers have been killed. The force is unlikely to stop another full-scale invasion. In that event, its task would be to hold off until help arrived. The Timorese presume it would, in contrast to 1975 when the West gave tacit approval to Indonesia's invasion. But most East Timorese think it is unlikely that Indonesia will ever come again. The first invasion caused it huge problems, international opprobrium and vast expense. And as the country threatens to disintegrate, its army has its hands full enough already.

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Trafficking in Central Asian women

The rise in vice

Jun 14th 2001 | ALMATY
From The Economist print edition

Lure of the West

THE number of Central Asian women going abroad to work as prostitutes is on the increase. In Russia and the former communist countries of Eastern Europe, most women are probably aware that the promise of a well-paid job as a waitress or dancer in a West European country may simply be a ruse to entice them into prostitution. But in post-Soviet Central Asia, where authoritarian governments try to control their citizens' knowledge of the world, not everyone is so sophisticated.

Of the Central Asian countries, Kazakhstan gets most credit from international experts for trying to protect its women from traffickers in prostitution. Kirgizstan is working on a "plan of action". Tajikistan is just beginning to attend to the problem. Uzbekistan and Turkmenistan see no need for public discussion. The prevailing attitude seems to be: "In our countries, there are no problems, so you can also not speak about trafficking."

The International Organisation for Migration estimates that up to 4,000 women were recruited into prostitution abroad from Kirgizstan in 1999, and 1,000 women from Tajikistan in 2000. Kazakhstan's foreign ministry says it helps about two women a week to escape from prostitution and return home.

The main destinations for Central Asian women are the United Arab Emirates and Turkey, with which the mostly Turkic-speaking countries in the region have cultural and economic ties. But there is also trafficking between the five republics. Tajik women are known to have ended up in Uzbekistan, a place they consider more stable than Tajikistan. Uzbek women, in turn, have been brought to Kirgizstan and Kirgiz women to Kazakhstan, which is also popular as a transit country because of its flight connections from Almaty.

In Tajikistan and Uzbekistan, countries of close families where tradition requires a woman to be a virgin when she marries, most unmarried women may feel safe from the enticements of traffickers. But a woman's home life in those countries and her limited exposure to the world beyond her family make her vulnerable should her husband neglect her, forcing her to work.

In Central Asia, it seems, the trafficking in women has cast suspicion on all their sex. Roza Aitmatova, president of Kirgizstan's Women Support Centre, remarks that these days "any woman who says she has been to the Emirates will receive knowing looks".

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Reform in China

Quick march, slow march

Jun 14th 2001 | BEIJING
From The Economist print edition

Is China scaling back its reforms?

ZHU RONGJI, China's prime minister, may have a reputation for being a straight talker, but he can still be hard to read. In a speech early last week, Mr Zhu admitted he was putting the brakes on some of the country's main efforts at economic reform because of the difficulties they were encountering. Yet at the end of the week he was giving the nod to an agreement with the United States that is meant to accelerate China's long-awaited entry into the World Trade Organisation (see article)—an event that Chinese officials admit is sure to put even greater pressure on some sectors of the economy.

The normal practice of most Chinese officials is to deny any shifts in policy, even when they are abundantly obvious. Yet a leaked text of an address given by Mr Zhu at Tsinghua University in Beijing on June 5th revealed the prime minister in a characteristically forthright mood, at least by the standards of his highly secretive government. Mr Zhu said it was necessary to "be safe and slow down somewhat a few major reforms in light of the current situation."

Mr Zhu indicated that one casualty would be the government's plans to promote badly needed tax reforms in the countryside. The aim of these is to eliminate various fees and levies arbitrarily imposed on farmers by local authorities and rely instead on a single tax based on income from crop production.

Farmers in many parts of the country are being forced by greedy, corrupt and impoverished local governments to pay ever bigger fees for such purposes as education and infrastructure. These often amount to over 10% of farmers' incomes, which have anyway been stagnant for the past four years. Growing numbers of peasants are petitioning higher authorities or taking part in mass protests against the levies.

As an experiment, China made changes to the taxes levied in rural Anhui province in early 2000. These have exacerbated other problems. A report by the State Development Planning Commission published in March this year found that in one Anhui municipality farmers had been given permission to keep nearly half the money they used to hand over to the government. But as a result the revenues of village-level governments had plummeted by nearly two-thirds—a devastating blow to an administrative tier that can hardly afford to support its bloated staff, let alone provide basic services for ordinary citizens. Across China, rural officials are nearly as demoralised as the farmers they are supposed to serve.

The original plan had been to extend the tax experiment to most of the rest of the country this year. But now, as the prime minister delicately put it, "it seems there are still some problems that need to be looked into." Other reforms to be slowed down (not for the first time) are plans to impose a fuel tax in place of the random charges imposed on vehicle owners by local governments, as well as the introduction of a social-security system that will remove the burden on employers to provide welfare benefits. The proposed tax would anger consumers at a time of rising fuel prices. Rapid changes to the social-security system would heighten fears among workers in state-owned enterprises—no less bitter than their country cousins—that they might lose some of the welfare provisions they once enjoyed.

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Afghanistan's failing opposition

The graceless victors

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From The Economist print edition

The bleak life of a Taliban town

THE town of Shibarghan in northern Afghanistan used to be one of the main strongholds of General Abdul Rashid Dostum, who was born there and who many hoped would be a match for the all-conquering Taliban. It was much fought over in 1998 in a battle bloody even by Afghan standards. But eventually the Taliban prevailed. Today their flag flutters over General Dostum's former home. A five-minute walk away is the town's sports stadium, where the general's men liked to show off their prowess. Today the stadium is empty, unused even for sporting activities, since the Taliban say sport conflicts with their strict interpretation of Islam.

The Northern Alliance, the grand name given to the remaining organised opposition to the Taliban, had hoped that General Dostum would rejoin their cause. In April he discussed this possibility with Ahmad Shah Masoud, the alliance's military commander. But the talks came to nothing and General Dostum is believed to have left the country again for exile. The general, a westernised Uzbek, was popular in Shibarghan and the surrounding area. Not for him the Taliban's ban on girls going to school. But General Dostum was an unreliable ally. For years he supported the communists when they ruled from Kabul. His forces and the Tajik Mr Masoud's have from time to time come to blows as a result of ethnic and political differences.

Mr Masoud still holds out in the Panjshir Valley, now a valley of fear. Sporadic opposition to the Taliban continues elsewhere in Afghanistan, but that is gradually being snuffed out. Yakowlang, a town of some 60,000 people, was reported this week to have fallen to the government. The alliance was cheered up recently when it shot down an elderly Soviet-made Taliban jet fighter. But this is hardly the kind of event to tilt the balance on the battlefield. Kept from annihilation by supplies from the Russian garrison in neighbouring Tajikistan, the alliance's policy appears to be one of holding on in the hope that the Taliban will become exhausted. It is expected to attack major roads with the aim of disrupting the Taliban's supply routes. Roads linking Kabul with such cities as Mazar-i-Sharif in the north and Herat in the west would be targets.

The Taliban are unpopular rulers. Virtually bankrupt, they have been able to do little for those hit by the past three years of drought. Their friendliest neighbour, Pakistan, provides unofficial help but cannot conduct trade officially, since that breaches United Nations sanctions, imposed because of Afghanistan's protection of Osama bin Laden, who is wanted by America on terrorist charges.

Many western countries want to help the Afghan people, but any humanitarian aid is received by the Taliban without much thanks. A meeting of western donor representatives in Pakistan last week was told that some relief workers had been harassed by the Taliban's religious police. The old saying, biting the hand that feeds you, has taken on a new and sinister meaning in Afghanistan.

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The European Union and the Irish referendum

Could everything now go horribly wrong?

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From The Economist print edition

The no vote in Ireland's referendum on the Nice treaty has disturbing implications for the European Union

ET TU, Paddy? For European Union officials it was a bitter blow that Ireland—of all countries—should reject the Nice treaty. Ireland, which has received billions of dollars' worth in cash handouts from the EU; Ireland, whose wealth has soared over the past generation; Ireland, where 86% of the population say that their country has benefited from EU membership, against an EU-wide average of 47%. In Brussels there is much bitter grumbling about ingratitude. How could the Irish, latecomers to the EU club themselves, now reject a treaty designed to ease the entrance of a dozen newcomers?

It still seems unlikely that Ireland's no to Nice will stymie enlargement. When Denmark rejected the Maastricht treaty in 1992, its government negotiated some "opt-outs" from the bits of the treaty its public most disliked—and then won a rerun referendum. Something similar may well happen with Ireland, particularly if it is made clear that the treaty's military parts need not touch the country's cherished tradition of neutrality.

But, even if the Nice treaty is kept alive, the European Union will still face some unsettling questions. In particular, how much more political integration can the EU's citizens swallow? By a quirk of its constitutional law, Ireland is the only EU country obliged to submit Nice to a referendum. How many other electorates across the EU would reject it too, if given a chance? Quite a few, probably.

The same question is raised by the euro, Europe's single currency. Only Denmark has held a referendum on joining it—in which it voted to stay out. Yet opinion polls in some of the 12 countries about to pulp their own currencies suggest that people remain ambivalent about the change, even though it is now a *fait accompli*. In Germany, for example, a recent poll taken by the European Commission's own Eurobarometer found 47% in favour of joining the euro and 44% against.

What can be done to persuade so many queasy Europeans that integration is good for them? One solution espoused by many top Germans is simply not to hold referendums: indeed, Germany's constitution bans them. These European issues, they say, are too complex for ordinary people to judge properly; that is what their elected representatives are for. In time, the voters will come to see the advantages. As a senior German puts it: "If we had had a referendum on the Treaty of Rome in 1957, it might have been rejected because it raised the price of bananas."

This German attitude may be elitist, but so far history has vindicated it. On the other hand, the sort of integration now being urged across Europe is much more tangible than a customs union or a single market. Nobody living in the euro-zone will fail to notice the new currency when it comes in. Given that some of Germany's most traumatic and triumphant experiences this century have involved their currency—the hyperinflation of 1923 that helped bring the Nazis to power and the inexorable rise of the D-mark after 1945—it is certainly bold to go ahead with so far-reaching a change without first legitimising it through a referendum.

Divergent interests

Beyond that troubling gulf between elite and popular opinion lies another issue. Might the interests of

certain influential countries in the EU be changing in ways that make them less “pro-European”?

Ireland’s vote is a modest example. When Ireland joined the club, it was a poor country in Britain’s shadow. Joining Europe gave the Irish a new confidence, new markets and lots of financial aid. But they are now so rich that by 2006 they will become net contributors to the EU’s budget. Expanding the club could raise Ireland’s bill further, since it will ensure that there are fewer farm subsidies to be had. Such considerations may sound ignoble, but voters are not obliged to be altruistic.

Besides, Ireland is not the only small country to fear that the EU, which has always been shaped explicitly to protect small countries’ interests, may be changing its nature. In a still bigger EU, more decisions will have to be taken by majority vote; small countries will find that their relative weight goes down. It was noticeable at Nice that the two countries that came closest to walking out—Portugal and Belgium—were both small.

But big countries are reassessing their stake in the Union too. When the EU got going, it was easy to pin down the national interests driving Europe’s big powers. After three horrific wars, France could create a new political arrangement based on absolute equality with Germany. Germany and Italy could win political rehabilitation after Nazism and fascism. Britain joined in the 1970s partly because it felt its economy was falling behind the rest of Europe’s. And, when Spain joined in the 1980s, the EU offered it a chance to emerge from the isolation and backwardness of the Franco era.

But such calculations may be changing. The French are clearly spooked by the idea that a bigger EU will be dominated by Germany—one reason why they fought so hard at Nice to preserve their parity of voting weight with their bigger partner. Germany’s elite is more excited by the prospect of enlargement and closer integration, but it is not clear that ordinary Germans regard the ditching of the D-mark and the opening of their country’s borders to eastern immigrants as an acceptable price to pay. Since it is no longer the sick man of Europe, Britain is more free to agonise about integration’s political costs—and has been indulging this freedom flamboyantly for at least a decade. And a more prosperous and assertive Spain clearly worries about the economic and political costs of enlargement.

Since so many of these calculations revolve round enlargement, it is safe to say that the Irish rejection of Nice will not be the only EU crisis provoked by the Union’s decision to take in new members. And enlargement is just one of three big tasks the EU has set itself. In less than six months’ time, two more will crop up: the euro will replace national currencies, and the EU’s members will undertake a constitutional debate, set to culminate in 2004.

Trying to do all these things at the same time runs daunting risks. Yet the EU has been through many crises since 1957—and has kept up the momentum for “ever-closer union”. The British, in particular, have always been inclined to predict failure, underestimating the sheer determination of the other Europeans to make the Union work. Certainly, anyone betting against the EU over the past 50-odd years would have lost a lot of money. On the other hand, as the Union takes up ever more ambitious challenges, it is beginning to resemble a gambler on a long run of luck, who keeps pushing his pile of chips back out on to the table.

Hopes and fears of EU countries

	Biggest hope	Biggest fear
Austria	EU forgets about Haider	Mass immigration from east
Belgium	Brussels as capital of new superpower	Brussels secedes, Belgium disintegrates
Britain	EU becomes giant free-trade area	Britain submerged into European superstate
Denmark	EU integration stops	Welfare state dismantled by EU
Finland	EU security arm ends Russian threat	EU-Russian antagonism
France	EU as French-led superpower; humiliates US	EU as German-led superpower; humiliates France
Germany	Federal Europe solves "German problem"	Popular backlash in Germany against euro or enlargement
Greece	EU admits Cyprus, screws Turkey	Turkey joins EU, screws Greece
Ireland	Continued boom on back of EU	EU ends Irish neutrality
Italy	Totally federal Europe	Kicked off top table for being too flaky
Luxembourg	More EU jobs	EU ends tax-haven status
Netherlands	Dutch model adopted by EU	Squeezed between France and Germany
Portugal	Catches up with EU economically	Small countries marginalised
Spain	Lots more EU money	No more EU money
Sweden	EU becomes more honest and Swedish	Sweden becomes more corrupt and European

	What they say about themselves	What others say about them
Austria	Badly misunderstood	Watch those neo-Nazis
Belgium	We have lots of good ideas	Tiresome zealots
Britain	We are the only country that obeys the rules	Make your mind up or leave; America's stooges
Denmark	Nobody understands us	Please stop having referendums
Finland	We're no trouble, not like those other Nordics	No trouble, nice phones
France	We invented the EU and we are the only people who understand it	Arrogant
Germany	We pay all the bills; we should have more say	Alarmingly ambitious
Greece	We are Europe's eastern outpost	Levantine rule-breakers
Ireland	We are the EU's economic stars	They owe it all to us
Italy	We are Europe's true believers	Dodgy politics, dodgy finances
Luxembourg	This is our stage	Too powerful for a micro-state
Netherlands	We are founder members; we deserve more respect	Know-it-alls
Portugal	Don't confuse us with Spain	Poor but honest
Spain	We are one of the EU's leading nations	Greedy
Sweden	We are the truest democrats	Self-righteous

Source: *The Economist*

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Ireland's no to Nice

Ahem, Ahern, a horlicks

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Critics of the EU treaty ran a strong campaign, its backers a lousy one

ONLY a third of Ireland's 2.9m voters took part in the referendum on June 7th, and only a bit over half of those said no. But that was enough to send the European Union into a tizzy: Irish voters had rejected the EU's Nice treaty, their leaders cannot ratify it, and the treaty, a necessary prelude to the EU's enlargement, cannot come into force until they do. Why did this usually Europhile nation thumb its nose at Brussels, its own government and main political parties, its employers and trade unions, its bishops and farmers, and many forecasters too?

One reason was that many voters did not understand the treaty, and could not see why they should bother. And of the few who did bother 54% joined its critics, a loose alliance comprising the Green Party, the ultra-nationalist Sinn Fein (the political wing of the IRA), conservative Catholics, pacifists and Eurosceptics in general.

All argued that institutional changes proposed in the treaty would reduce Ireland's influence in the EU. They raised fears of a two-tier EU superstate, and underlined and overstated the threat that plans for an EU rapid-reaction force posed to Ireland's neutrality. Money too was at stake: more for new, poor, farming East European countries must one day mean less for no-longer-poor, farming Ireland.

The no vote also reflected worries about the EU that went wider than the treaty. Over the past year, ministers of Bertie Ahern's government have criticised the EU's increasingly centralised decision-making. Mary Harney, the deputy prime minister, who heads a small free-market party in the ruling coalition, has argued that Ireland is closer to Boston than Berlin in its style of economic management. Ireland has been scolded by some EU countries, notably France, for its low corporate tax regime. Its fiscal policy has been censured by the European Commission as too loose. Maybe, but given Ireland's boom, it all seemed unfair.

On their side, the yes campaigners fell victim to their own complacency. They underestimated their opponents and failed to mobilise their own supporters. The pro-Nice parties between them took 85% of the vote in Ireland's 1997 general election. But in the referendum campaign they were barely to be seen, preferring, it seemed, to save money for the next general election, due within a year.

For Mr Ahern, who said at the campaign's outset that rejection of the treaty would be "a deep embarrassment and national humiliation", the result, personally, is both. His political judgment had plainly gone walkabout. Still, he intimates that he will try to ratify Nice in the end. Ireland will not seek changes in the treaty, which it would not get, but reassurances about it. Then, after winning (he hopes) a general election next year, Mr Ahern would call a second referendum—and launch a much more vigorous campaign for the treaty.

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Italy's new government

Tutti frutti

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Silvio Berlusconi's new government contains some formidable operators—and some awkward customers too

IN THE past nine years, since the old system dominated by Christian Democrats collapsed, Italians have got used to governments that have included a hotch-potch of different kinds of people—ex-Communists, Greens, Catholics, technocrats—more often than not led by a prime minister who has been little better than *primus inter pares*. Not this time. Silvio Berlusconi is plainly the boss, with a cabinet very much to his own taste. Unusually, he has also ensured that the leaders of the main parties in coalition with him, Gianfranco Fini of the post-fascist National Alliance, and Umberto Bossi of the once-separatist, now-federalist Northern League, have big posts in government too: the first as deputy prime minister, the second as minister for institutional reform and devolution, two areas where the previous centre-left government made little headway.

Reuters

Berlusconi's boys: Rocky Ruggiero and trusty Tremonti

This is a smart move. In the past, Italian party leaders have stayed out of government, sniping and manoeuvring from the wings. Last time Mr Berlusconi was in power—in 1994, briefly—the Northern League was in coalition with him but Mr Bossi undermined the government and then dished it. This time Mr Bossi will be more tightly boxed in. He wants northerners to pay less in tax and the government in Rome to leave them generally alone. He may even go on being rude about Italians who live south of the River Po. But he must get along with a Sicilian, Enrico La Loggia, the minister for regional affairs.

The ministers likely to carry most weight and enjoy most freedom are those with briefs in areas outside Mr Berlusconi's own range of experience: Renato Ruggiero at foreign affairs and Antonio Martino at defence. Mr Ruggiero has been a diplomat, minister for foreign trade, ambassador-at-large for the Fiat car-making conglomerate and, until recently, the boss of the World Trade Organisation. A tough negotiator (he is "Rocky Ruggiero" to those who had to bargain with him), he knows the ways of the world (and of his mentor, Giovanni Agnelli, Fiat's grand old man). Mr Ruggiero is a free-trader who is keen on the European Union—and wants to widen it to the east. He is unlikely to give Italy's EU partners any nasty surprises.

Mr Martino is different. Son of Gaetano Martino, one of the European common market's founding fathers, he was foreign minister in Mr Berlusconi's first government. More notably, he is one of a rare breed in Italy: a true liberal in the 19th-century sense, a nation-state man who—by Italian standards—is wary of EU integration. He likes Margaret Thatcher and has friends in the new American administration. Indeed, a word from the White House may have encouraged Mr Berlusconi to give him the defence job. The new interior minister is a Ligurian, Claudio Scajola, rewarded for his clever orchestration of Mr Berlusconi's election campaign, including the adroit way he dealt with other parties and divided up the seats between them.

As expected, Giulio Tremonti, a rich tax lawyer who was finance minister in 1994, gets a beefed-up Treasury, with economics and finance merged for the first time. He will be the first Italian minister in charge of both raising and spending the country's cash. Until a few years ago another minister presided over the budget; this, too, will be Mr Tremonti's responsibility. The new economics supremo is also credited with having persuaded the Northern League to accept the deal that ties it more tightly this time into the governing coalition.

Other ministers include Letizia Moratti, a former strong-willed boss of state television who has also worked for Rupert Murdoch and now becomes education minister; Roberto Maroni, Mr Bossi's faithful deputy, who will head the labour ministry; Roberto Castelli, another Northern Leaguer, who becomes justice minister. Giuliano Urbani, an academic who may actually have dreamed up the idea of Forza

Italia, Mr Berlusconi's party, in 1993, will oversee art and culture—a bigger job than it used to be, since Italy, under go-ahead ministers in the two previous leftish governments, has begun to promote itself as an artistic superpower.

The most controversial appointment is Mr Bossi's as minister for devolution. The new government may be the most northern-slanted in Italy's history. Eight ministers, including the boss, come from just one of Italy's 20 regions: Lombardy, which is the country's richest—and has the most go-getting, can-do attitude. So the question is: will the Lombards change Italy, or will Rome change the Lombards?

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Charlemagne

Jack Straw

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Britain's new foreign secretary is a very English Englishman

Get article background

TO BRITAIN'S progressives these past four years he has been Mr Nasty Guy: the home secretary—in plain European, minister of the interior—who loved to keep out asylum-seekers; who smothered dreams of a genuine freedom-of-information law and brought in a phoney one; who wanted to limit the right to trial by jury and was already pushing up prisons like mushrooms to hold the startling number of Britons who are sent there anyway. He was also the minister who handled the incorporation of the European Convention of Human Rights into British law. But he got little credit for that; it merely damned him in the eyes of conservatives who see the convention as a foreign plot to let crooks go free and give IRA gunmen compensation for not being arrested with kid gloves. And now, hey presto, Jack Straw has changed hats: out, a week ago, went the bug-eyed but Europhile Robin Cook, and in came Mr Straw to speak for Britain to the world. In particular, to the EU—a union for which, until now, he has expressed no visible enthusiasm whatever.

So what does Tony Blair's new foreign secretary bring to the council table? Could his appointment be a heavy hint to other EU countries that their recalcitrant British partners plan to be even more stroppy than before? No. Whatever Mr Blair's reasons for shifting Mr Cook—the latter's friends and enemies will offer you quite a menu—this was not one of them. In Britain's general election on June 7th, Mr Blair has just ground into the dust a Conservative Party whose slogan was "In Europe, not run by Europe", and even that by the end of the campaign had begun to sound almost Europhiliac, set against the off-message hostility of many Tories, not least Margaret Thatcher. In contrast, the EU-ardent Liberal Democrats are riding high, whereas the United Kingdom Independence Party, although it has three members in the European Parliament, is not even visible in the dust. At this moment, Mr Blair no more needs to pander to Britain's Eurosceptics than to the Grand Cham of Tartary.

Mr Blair, however, was not born yesterday. He knows that moments pass, and that the British public, little as it loves the Tories, loves the EU's single currency even less. And he is sworn, at some unspecified date, to a referendum on that issue. There is also one force that he need not pander to, but cannot ignore: his finance minister (and rival) Gordon Brown, who will accept membership of the euro-zone when the Treasury's five economic tests for doing so are met, maybe, but not a day before. Who better to put in charge of Britain's European policy than a loyal ally, and one who cannot be accused of letting any private passion for the EU outweigh his duty to the public interest?

Not that Mr Straw's career, on the face of it, reveals any passion for foreign affairs, in any direction. Twenty years ago, it is true, he was a stalwart of Labour's anti-European wing. Yet in the string of posts as spokesman on this and that which he held from soon after he entered Parliament in 1979 until he won high office in 1997, none looked out to the wide world. Here, however, is an adaptable man. Born in 1946, as a schoolboy he was a marcher against Britain's nuclear weapons, in the 1970s a councillor in a London borough widely known as "the Socialist Republic of Islington". By the mid-1980s he was, accurately, denouncing his party's then anti-nuclear stance and its "loony-left" local councils as making it unelectable. As home secretary, he let Britain's police arrest Augusto Pinochet in 1998, but he was happy later, on grounds of health, to let the general go.

And whatever his lack of passion, ignorant of the EU Mr Straw is not. When its interior ministers have met, there for four years he has been—"co-operative, innovative, constructive, better prepared than almost any other British minister," says a British Euro-addict. A "formidable" member of the ministerial council, says an EU commissioner. For a senior politician, Mr Straw is unusually ready to listen. Few doubt that, having listened, he will be rapidly in command of his wider briefs— though it will take some doing to match Mr Cook's grasp of the Balkans—before deciding, firmly, what's best for Britain and (how could there be a difference?) for Labour and Jack Straw.

Down-to-earth, up from Essex

Do not mock: that happy coincidence of interests might be a real one. Britain's voters may be right or wrong about what is best for them, but they and Mr Straw think much alike. They do not want asylum-seekers in their country or liberalism in their interior ministry. They value the jury system, but they value a "guilty" verdict on the guilty more. The all-informed press that most of them want is the tabloids. Likewise, they do not want to be run from Brussels, but they are not mad keen on Whitehall either. And though they prefer the pound to the euro, few of them, witness the election, would go to the barricades to save it.

Not by chance does Mr Straw share this down-to-earth outlook. He is that rarity in the first Blair government, a very English Englishman: son of a clerk and a teacher, pacifists both; council-estate childhood just outside London, the Essex side, the one where the nobs do not live; parental divorce; then the usual path upward for the unusual cut-above-working-class youth of the 1960s—state-aided independent school, red-brick (Leeds) university, student politics, the Bar, political aide in 1974 to flaming-red Barbara Castle at the mud-grey department of social services. Divorced and remarried himself by 32, Mr Straw knows how the real world lives. If there is a whiff of "old Labour" about him, it is that of practical social betterment, not the dream-world leftism that (as Islington must have taught him) seldom achieves it.

Organised betterment, that is: Mr Straw is a manager, a man of performing government. ("Freedom of information? That's for oppositions," as one watcher quotes him.) How high he may hope, at 54, to manage himself, who knows? He keeps his cards close to his chest. Still, for what is visible, says this watcher, "with Jack Straw, what you see is what you get."

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Bulgaria's election

An ex-king for ex-communists?

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Simeon II looks likely to win power

FOUR years ago, Ivan Kostov was Bulgaria's white knight, his mission to revive the economy from the financial collapse inflicted on it by the ex-Communist Bulgarian Socialist Party (BSP). Four years on, he has done it. Yet Mr Kostov's armour is looking pretty grubby. And the new white knight is a former king—and maybe future prime minister, nay president.

EPA

Exiled as a boy king in 1946, and a permanent possibility in Bulgarian politics ever since 1990, Simeon II—or Simeon Borisov Saxe-Coburggotski, to use the name in his passport—entered the political fray in February. The latest poll gives the movement he set up 37.5%, putting it far ahead of the only other group likely to qualify in the general election on June 17th for any seats at all: Mr Kostov's United Democratic Forces (a coalition dominated by his own Union of Democratic Forces) with 18%, the Bulgarian Socialist Party (BSP) with 16%, and the mainly ethnic-Turkish Movement for Rights and Freedoms with 5%. Other polls disagree in detail, but the ex-king's Simeon II National Movement looks likely to win the most seats, perhaps even an absolute majority.

Why? With help from multilateral lenders and a currency, the lev, pegged since 1999, through a currency-board system, at just under two to the euro, the Kostov governmenthas indeed stabilised the economy. It has privatised a lot—but mostly to politically favoured managers and dubious investors, foreign or local. Unemployment is a high 18%, living standards still low. Sleaze is widely assumed to be rampant; Mr Kostov's attempts to distance himself from it have come late. And the BSP, its economic incompetence still fresh in voters' minds, is no real alternative.

The ex-king's message, put out in early April, was simple (or simplistic): honesty and new faces in public life, harsh measures against corruption, a huge improvement in living standards within 800 days. The details, filled in since, are not altogether convincing.

His new faces are a curious collection: media and cultural figures, lawyers, young investment bankers with experience abroad, businessmen linked to local economic groupings. Egos abound, and often clash. Simeon himself is an exception. Self-effacing and evasive, he will not even be standing for parliament, perhaps because it would involve swearing allegiance to the republic. Nor will he say whether he would become prime minister if his movement were to win the election, though he has hinted he might challenge President Petar Stoyanov in the election for that post due this autumn. It would require constitutional amendments: till recently, Simeon lived in Madrid, and the rules require five years of continuous residence.

As to policy, the movement's programme, unveiled only last month, is orthodox free-market stuff: the budget balanced, licences abolished, bureaucrats laid off, taxes cut and rejigged to woo private enterprise and investment, easy loans for small firms, capital markets developed. But the main doubt concerns post-electoral politicking more than policy. Simeon says he is for a coalition government, even if his movement wins an overall majority, but one with people who share the same principles. Mr Kostov says he is willing, provided the ex-king backs Bulgarian membership of NATO—as Simeon seems to, though a good many Bulgarians do not.

Conspiracy theorists say it is all an elaborate pantomime, backed by "powerful European interests"—Bulgaria is also a would-be EU member—to exclude the BSP. If so, the script is less than perfect: the mayor of Sofia, Stefan Sofianski—caretaker prime minister in early 1997 and long seen as a potential rival to Mr Kostov—has been getting ready to lead his groupinginto coalition with Simeon if Mr Kostov will not.

The Simeon II movement too looks apt to split, sooner or later. But that could mean later if the economy perks up a bit. Meanwhile, an ex-king looks likely at least to be sharing power in a republic that was communist-run only a dozen years ago.

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Divided Macedonia

War clouds gather

Jun 14th 2001 | ARACINOVO
From The Economist print edition

Worry grows that Macedonia may descend into all-out civil war

Get article background

WHEN they surfaced last weekend in this suburb of Skopje, the Macedonian capital, Commander Hoxha and the dozen or so ethnic-Albanian fighters in his entourage looked like cats with a limitless supply of cream. Squinting in the hazy sunshine, they pointed their sniper rifles at tower blocks in the nearby city and defied their foes to come and get them.

By midweek, as fighting broke out for control of several nearby villages, their smart black uniforms had become a bit dishevelled. But, unmistakably, it is the rebels of the National Liberation Army who are calling the shots, in more than the literal sense, in Macedonia's conflict.

They were not, of course, represented at the emergency consultations on Macedonia held by NATO's leaders in Brussels on June 13th; nor even at the talks scheduled for the next day in Skopje between Macedonia's Slavic and ethnic-Albanian politicians and envoys of NATO and the European Union.

But in both places the mounting challenge from the NLA was setting the tone of increasingly frantic deliberations about the political future of Macedonia, which the rebels want to remake as a sort of bicommunal state. The fighters' threat to fire a few mortar rounds at the capital or the airport, entirely credible now that they are positioned half-way between those two places, has concentrated minds.

The rebels' advance has also hastened the flow of civilians out of mixed areas and spurred efforts to bring about a ceasefire. On June 11th the government forces agreed to stop shelling villages in the north of Macedonia, near Kumanovo, where rebels and thousands of non-combatants had been holed up. But that left only the tiniest opportunity for peace in a conflict that has already displaced about 70,000 people and reduced five villages to ruins, though it has claimed relatively few lives—perhaps two or three dozen.

On both sides of Macedonia's ethnic divide there is a sense that closer involvement by western peacekeepers, whether under the aegis of NATO or simply a coalition of countries willing to take part, is the only way to halt the slide towards all-out war. Behind a smokescreen of reassuring language, which insists that the NLA is a small band of extremists and that all is more or less under control, the western countries whose troops protect nearby Kosovo have been pondering what to do.

Britain is being urged to do the lion's share of any peacekeeping tasks that may arise in Macedonia. On past form, these might include an effort to "demilitarise" the new war zone by persuading the NLA to hand over its weapons, or at least some of them. As a first step, a British battalion has been deployed near Prizren in southern Kosovo, hitherto policed by Germans and Turks.

Though extremely wary of an open-ended involvement in yet another Balkan quagmire, NATO commanders draw some comfort from the recent success of their plan to bring an end to a low-level guerrilla campaign by ethnic-Albanian rebels in a strip of southern Serbia to the east of Kosovo, near Presevo. The fighters were induced to leave the area and hand over several truck-loads of arms, as the Yugoslav army reasserted control in close co-operation with NATO, its old enemy. But the rebels in Macedonia seem better armed and less amenable to pressure than their ethnic-Albanian cousins in Serbia.

And if western forces do become more involved in Macedonia, what exactly would they do? As suspicion between Slav and Albanian deepens by the day, there is huge disagreement over the terms of any international operation. The Slav leadership would like more military advice and hardware to help defeat the guerrillas. For their part, even moderate ethnic-Albanian politicians see future NATO intervention as a way to legitimise their community's control of a large swathe of the country's north and west, including the entire border with Kosovo.

In one sense, NATO is already deeply involved in Macedonia: the country is a vital supply route and logistical base for peacekeepers in Kosovo. If necessary, NATO could make alternative arrangements, especially now that its relations with Serbia are improving fast. But could the West really remain indifferent to another, escalating ethnic war in the southern Balkans, a stone's throw from a NATO member, Greece, and from would-be allies like Bulgaria and Romania? No.

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Dirigisme in France

Don’t sack your workers

Jun 14th 2001 | PARIS
From The Economist print edition

The French government is making life harder for employers

CAUSE and effect? Last weekend thousands of banner-waving French workers marched through Paris, denouncing companies such as Marks & Spencer that lay off workers without adequate consultation. Four days later, on June 13th, the National Assembly, in pursuit of “social modernisation”, amended its labour laws to make it still harder for employers to make “economic redundancies”. The minister of labour pronounced herself “very happy”; the leader of the assembly’s Communists said the world of work had made “important advances”; and bosses bemoaned the perils of political expediency.

The bosses have a point. After all, the chain of consequences is rather longer than a mere four days. It goes back to 1995, when the reformist ideas of Alain Juppé, France’s last conservative prime minister, provoked huge street demonstrations and, two years later, the conservatives’ defeat at the polls. And it will surely go forward to next spring’s presidential election and the presumed encounter between Mr Juppé’s Socialist successor, Lionel Jospin, and France’s incumbent conservative president, Jacques Chirac. Put simply, however loudly the bosses, caught between a slowing economy and ever-increasing foreign competition, demand flexible labour laws and lower social charges, Mr Jospin has no intention of upsetting the voters.

That, in turn, means he can ill afford to upset the Communists. They may be electorally weak—in local elections three months ago their vote collapsed—but they are part of Mr Jospin’s coalition and to have them vote against their partners would insult the prime minister’s reputation as a political manager. Unfortunately for Mr Jospin, such behaviour is likely to become ever more tempting for the Communists: the lesson they draw from the local elections is that to revive their support they need to revert to the hardline tradition of the class struggle. Hence this week’s vote: it should have taken place two weeks ago but had to be postponed as the Communists twisted arms fiercely enough to get a legal wording that they could live with.

How much difference the wording will make is hard to say. What has prompted new legislation on “social modernisation”—jargon for improving relations between workers and employers—is a rash of layoffs at a time when the French economy is doing better than any other in the euro-zone. In 1999, for example, Michelin, a tyre-maker, announced large layoffs even as it reported record profits. Mr Jospin protested, but did nothing. This year layoffs have already been announced or mooted at Marks & Spencer, Danone, Moulinex, AOM, Valeo and other big companies.

In the boardroom, such job losses are seen as a rational response to tougher competition, bad exchange rates and other realities of the global market. On France’s shopfloor—and in Mr Jospin’s government—they smack of the “economic self-interest” of businessmen wanting to boost shares or satisfy foreign pension funds.

So the government’s remedy is not the looser labour law craved by the employers, but a tighter one: assuming a company is not confronted by impossible circumstances or by irresistible technological change, it can announce “economic redundancies” only after “all other means” have been tried to preserve jobs. Moreover, it will have to negotiate with a works council authorised to offer other solutions and, if deadlock ensues, submit to the arbitration of a government-approved mediator.

How will such legislation work in practice? One businessman sourly notes that of the seven countries in which Marks & Spencer has announced layoffs only France has felt compelled to legislate. He predicts a fall in foreign investment in France and a drop in its competitiveness.

Maybe so, but not until after the election. In the meantime Mr Jospin is intent on winning that election. Witness this week not just more “social modernisation” but also a promise that from next year new fathers will be able to take two weeks’ state-financed leave. Of course, after the election, the arithmetic

could all come adrift and the workers may take to the streets again. But the difference would be that a President Jospin and his prime minister will have five clear years with almost no elections to worry about.

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Conservative politics

Foreigners in their own land

Jun 14th 2001
From The Economist print edition

The Tories are down but not out

A SECOND landslide defeat has left the Conservative Party bewildered. The leadership election in which it is now engaged is not just a search for a new leader but also for a new inspiration (see article). The oldest and most successful political party in the world, "the natural party of government" as it sees itself, has rarely been further from power.

Last week's election result speaks for itself. After four years of opposition, the party managed to gain only one more seat in Parliament. Although it gained two percentage points (to 33%) in the popular vote, this figure still represents merely its second-lowest share of the total votes cast since 1880. And, more tellingly, the actual number of votes cast (8,352,845) for the party was the lowest since the mass franchise was introduced in 1929.

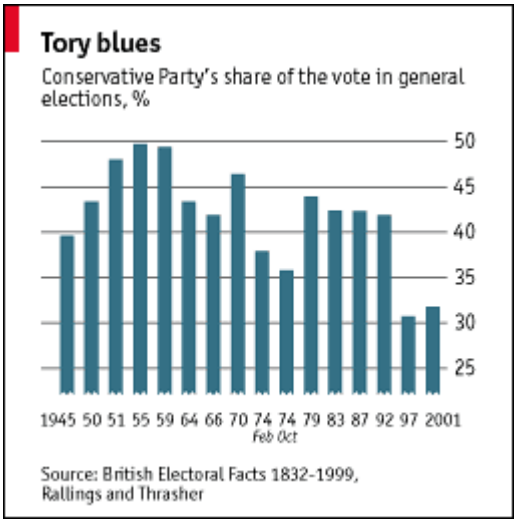
No wonder that party leaders have been calling for a period of "reflection". The swing needed to overturn the Labour majority in five years' time looks daunting. Yet those who in the past have written off the party have always been proved wrong. Not for nothing did its most recent historian, John Ramsden, call his book "An Appetite for Power" (HarperCollins 1998).

Years in the wilderness are not a new phenomenon for the Conservatives. In 1830, they lost power over the first Great Reform Act, and the party did not form a majority government until 1841. After the split over the Corn Laws in 1846, the party did not enjoy a majority in government until 1874. After the catastrophic defeat of 1906, it did not return to government until 1915. And after the 1945 landslide, it was out of office for six years.

After every big defeat the same questions have been asked about the party's continuing relevance. After 1906, many doubted that a party founded to represent the interests of the landed aristocracy in the late 18th century could possibly survive in the age of mass democracy.

In fact, the party proved itself the master of the mass electorate. After each defeat the party has re-invented itself. Above all, its politicians demonstrated a ruthless appetite for power, subordinating all other considerations, which resulted in the ditching of whoever happened to be the unfortunate leader at the time. The party has always prided itself on being the non- or even anti-ideological party and has seen itself more as a pragmatic exercise in statecraft. This is founded on an inherent Tory belief

that the party is a party of government, or it is nothing.



Given that appetite for power, there is every reason to believe that the Conservatives will revive. But they will need to cast off old certainties and re-engage with the electorate. As Mr Ramsden writes, "there has almost been an inverse correlation between the Conservative Party leadership's intellectual clarity and its electoral record of success". Before each big crash, the party has been captured by a wing of the party, be it die-hard anti-reformers in 1830, protectionists in 1846, tariff reformers in 1906 or appeasers in 1945. This wing, arguing its case with passion and conviction, has taken over the party, only to see the party then subside into minority isolation within the political nation as a whole.

The leaders who led the party out of these ideological cul-de-sacs were all prepared "to sacrifice some clarity to the belief that unity and diversity were more important". And each of those leaders, such as Disraeli, Salisbury, Baldwin and the "Butskellites" of the 1950s were able to win office for long periods of time. All these leaders were pragmatists, able to shift the party's agenda on to new concerns, not necessarily healing the wounds of the past but uniting the party around the issues of the present.

Crucially, leaders such as Baldwin and Disraeli were able to present a narrative of change and flexibility, and yet link these qualities to eternal Conservative verities such as nationhood and stability. It is also true that those thinkers and politicians who have been best at plotting a new course for Conservatism, such as Burke and Disraeli in the 19th century and Hayek in the 20th, have been foreigners or outsiders. Their detachment has given them the clarity that has often been lacking in their more blinkered, true-blue colleagues.

How does this reading of history account for the phenomenon of Lady Thatcher? In the coming weeks, many MPs will be holding her up as a shining example of what can happen if the party fights on a set of clear ideas. But this would be to ignore three crucial facts. First, she was much more cautious in her early years as prime minister than her acolytes now like to remember. And once she shed that caution after 1987, she became an electoral liability. Second, her success in the elections of 1983 and 1987 in winning parliamentary seats was not based on increasing the overall Conservative share of the vote. Her victories depended on the split between the Labour, Social Democratic and Liberal parties. Lastly, her period of electoral success disguised a collapse in the mass membership of the party that has never been seriously addressed.

Even allowing for the overall decline in political party membership, the loss of 600,000 members in a generation, more than half the membership, is still a huge fall. Thatcherism may have gone down well with the activists, but it failed to appeal beyond them. Much like Mr Hague's brand of Conservatism at this election.

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Ministerial reshuffle

Blair's new world

Jun 14th 2001
From The Economist print edition

All change. But to what end?

Reuters

We are still friends, honest

STUNG by voters' criticism of his first term, Tony Blair has embarked on the biggest upheaval Whitehall has seen for years. He says he wants the reshaped bureaucracy to deliver, and fast. But his ministerial reshuffle reveals, on the two big issues which will determine the success or failure of his second administration, a two-speed government. On the first—relations with the euro—the pace will be slow and tentative. On the second—delivering better public services—ministers will have to gallop. Yet economic turns of fate and Whitehall conservatism may still frustrate him despite his 167-seat majority.

The replacement of the euro-enthusiastic Robin Cook as foreign secretary by the euro-pragmatic Jack Straw (see article) is a sign of the caution with which Mr Blair is approaching a decision on joining the euro. Downing Street aides tried to soothe Mr Cook's pain at his demotion to the leadership of the House of Commons by lauding his formidable parliamentary and debating skills. But Mr Blair had evidently become tired of the soap opera of euro tussling between Mr Cook and Gordon Brown, the chancellor.

This leaves Mr Blair as reliant on Mr Brown as ever. Some close observers claim to detect a distinct cooling of the relationship between the two. Ministers who work with both insist that this talk is media babble. "New Labour was Gordon and Tony's creation," says one minister. "If they fall apart, New Labour falls apart and they both know it."

Far from shoving Mr Brown out, the reshuffle seems in fact to bring him in closer. Apart from getting rid of Mr Cook, a major irritant, it has brought back Brown loyalists sacked in the first term, such as Harriet Harman, now given the job of solicitor-general. Young Brown protégés, such as Douglas Alexander, who helped run the election campaign, have been rewarded with junior ministerial jobs.

In truth, Mr Blair needs Mr Brown to deliver the economic growth and hence the tax revenues to pay for the increased cash he has promised will go to public services. But money alone does not ensure improvement. That is why Mr Blair has been persuaded to abandon his reluctance to interfere with Whitehall structures.

David Blunkett, the new home secretary, takes on a greatly shrunken department. The Home Office will now deal solely with crime, punishment, race and immigration. Everything else, from electoral law to gambling supervision, has gone to other departments. The Ministry of Agriculture has paid the price for its mismanagement of foot-and-mouth disease and various food scares; it has been subsumed by environment with Margaret Beckett in charge.

Alistair Darling, a success at social security, has added employment to his brief in a new Ministry of Work and Pensions. This ends the time-consuming negotiations between two departments previously required in pursuit of the Blairite mission to link welfare benefits to requirements to seek work. Right across Whitehall, says a cabinet minister, the message is clear: "If you don't deliver, your unemployment notice will be on your desk."

Three things, however, could frustrate this dynamism. First, ministers in the merged departments will have to overcome deep-rooted bureaucratic conservatism. Mrs Beckett, for example, will have her work cut out stamping out the old producer-orientated mentality of the farming bureaucrats in order to put consumer interests to the fore.

Second, the enhanced policy “enforcement” role of the Cabinet Office, now under John Prescott, the deputy prime minister, could hamper rather than help delivery. Some ministers worry that, when set alongside the Treasury’s weapons for ensuring policy delivery, there will be far too much enforcement and too much time will be spent inspecting policies rather them making them work.

Finally, Whitehall high-flyers traditionally regard the making of policy as the supreme bureaucratic achievement and delivery of policy as an altogether lower form of life. Whitehall is long on thinkers, short of doers. But doers are what Mr Blair needs most.

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Public services

Taking on the teachers

Jun 14th 2001
From The Economist print edition

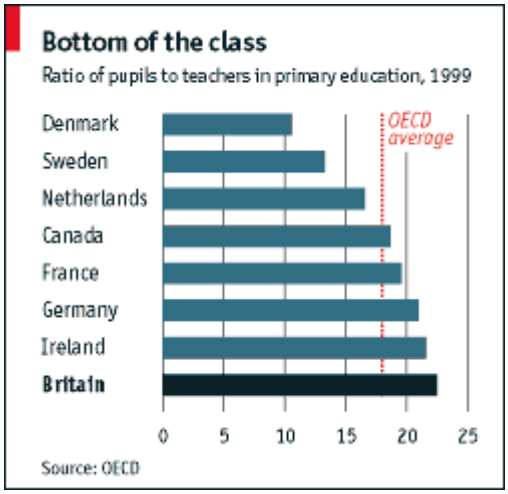
Can Tony Blair deliver on his promises to improve education?

IF EDUCATION, education, education was the soundbite for Labour's first term, delivery in triplicate is the overriding theme of Labour's second term. The electors were prepared to give Tony Blair a second chance to come good on the promise to achieve high-quality public services. They will not be so forgiving a third time round if performance remains lacklustre.

In Britain's schools, money is not the problem over the next three years. But the shortfall in spending compared with other countries remains substantial. International comparisons released this week by the OECD show that public spending on education in Britain was 4.9% of GDP in 1998, compared with an average of 5.3% for developed countries. Several countries, including Denmark, New Zealand, Norway and Sweden, devoted far more, between 7% and 8% of GDP. Even with the government's generous funding increases for schools, Britain's spending will only reach 5.3% of GDP in three years' time.

Big budgets help only if the money is spent effectively. "High spending does not necessarily mean high quality," points out Andreas Schleicher, in charge of educational statistics at the OECD. The top performers in international comparisons of maths scores for 13-year-olds are South Korea, Japan and the Netherlands. None of these countries is a big spender on education. The largest improvement in maths scores in the late 1990s occurred in the Netherlands, which spends the same proportion of GDP as Britain. Discouragingly, scores for British children did not improve over the same period, leaving Britain ranked tenth out of 12 countries.

If the government is to deliver better-performing schools, it will have to confront Britain's powerful teacher unions over pay and workload. Contrary to popular perception, teachers in Britain are well paid compared with their counterparts in other countries. Especially at primary schools, salaries are significantly above the average for other developed countries, contributing to unfavourable pupil/teacher ratios (see chart). However, even with the introduction of performance-related pay, salary scales do not deliver effective incentives for more experienced teachers. Nationally-agreed pay schemes do not provide sufficient compensation for the higher cost of living in London, leading to severe shortages of teachers in the capital. There is still too much rigidity in the system to attract the best teachers to the more difficult schools.



The other bruising battle that lies ahead for the government will be fought over an enhanced role for the private sector. When launching the manifesto, Tony Blair said that "no dogma" should stand in the way of reform of the public services and highlighted the intention to create "a diverse range and choice of state schools". The manifesto appeared to wave a green flag to the creation of new schools, which would be an important spur to competition.

This week, the Adam Smith Institute (ASI), a right-of-centre think-tank, called for a more far-reaching reform to combine public finance and private provision. All schools should become independent of local education authorities, allowing new ones to set up as long as they can attract pupils. "A wave of new schools is the best way to raise standards because it will force the closure of most of the bad schools," argues Madsen Pirie of the ASI.

In the Netherlands, three-quarters of children attend schools that are publicly financed but privately provided. Under this long-established system, the government ensures that money follows the pupil and schools compete among themselves for children. The vast majority of these schools are run as non-profit

institutions. They have to teach a national curriculum but are free to adopt their own approach in how to teach it. Such a system is sometimes supposed to lead to inequalities in attainment, but these are less in evidence in the Netherlands than in Britain. It offers a benchmark to measure whether Labour now delivers reform in office to match its rhetoric during the election.

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Social trends

High rollers

Jun 14th 2001
From The Economist print edition

Marketing dreams from New York to London

AFTER yuppies and dinkies, a new creature from adland stalks the block. The NYLON, an acronym linking New York and London, is a refinement of those more familiar categories such as jet-setters and cosmocrats (cosmopolitan aristocrats...do keep up). Marketing professionals have noted that despite the demise of Concorde, a new class of high-earner increasingly spends his or her time shuttling between the twin capitals of globalisation. And NYLONS prefer their home comforts on tap in both cities. Despite the impressive number of air miles, they are not adventurous people.

As distinct from Tom Wolfe's "masters of the universe" of the 1980s, NYLONS have done more than well out of the long boom and new economy of the last ten years. They are DJs, chefs, games designers, Internet entrepreneurs, fashionistas, publishers and even a select band of journalists and writers. They are self-consciously trendy and some are even able to afford houses in both cities. Others will put up with a house in one, and a view with a room in the other. Of course, their horizons do extend beyond just New York and London. For many, Los Angeles is an important shopping mall.

More significantly for adland, NYLONS provide some useful marketing savings. Campaigns no longer have to differ very much in the two cities, as NYLONS bring them ever closer together. The restaurants are the same, with Nobu now in London and Conran in New York. Many plays run in both cities at the same time, and DJs shuttle between the two, playing the same garage to the same people in similar clubs. *Time Out* and *Wallpaper* are the magazines of choice. All this is fine for NYLONS. But not so much fun for everybody else watching Notting Hill turn into a pale imitation of Greenwich Village.

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Election

New Britain

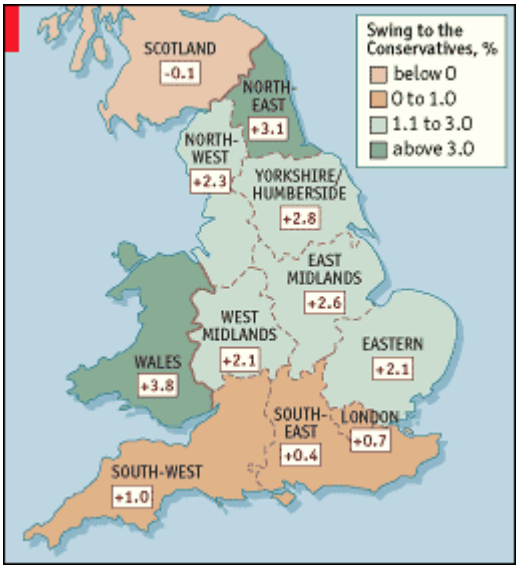
Jun 14th 2001
From The Economist print edition

Politics without class

ONCE upon a time, Britain was a country in which most people voted, many of them voting for the party they thought best represented their class. The result was that the electoral system ensured that power alternated between two big class-based parties, Conservative and Labour. That country no longer exists. New Labour has rewritten the script of British politics.

Ever since Tony Blair became leader, Labour has aimed to reach out beyond its traditional electorate, to the middle class and the south of England voter. The impact of that appeal was even more apparent on June 7th than it was four years ago.

As the map shows, apart from a poor Conservative performance in Scotland, the swing away from Labour since 1997 was lowest south of a line from the Thames to the Severn. The apple of the New Labour eye, the southern English voter, proved indeed to be the most loyal to Mr Blair.



Meanwhile, the swing away from Labour was also lowest in middle-class seats and amongst middle-class voters. Labour's vote fell on average by 3.6% in the most working-class seats, but by only 0.3% in the most middle-class ones. Equally, according to an ICM/BBC poll, Labour's vote rose by five points in the top AB social group while it fell ten points amongst the DEs. In short, the middle classes were loyal while the working classes defected.

Being in the centre has its costs. At 59% turnout was lower than at any time since 1918. And it was Labour voters who were most likely to stay at home. Turnout fell most in Labour heartland seats, even though they already had the lowest turnouts. There is now a double-digit difference between the turnout in the typical safe Labour seat and that in its Conservative counterpart. The ICM/BBC poll found that Labour supporters were twice as likely as Tory supporters to stay at home.

But voters staying at home in the party's safe seats did Labour no harm when it came to winning seats in the House of Commons. This was one of the reasons why Labour won a second landslide majority of 167 even though the party's lead in votes cast was a relatively modest nine percentage points. Labour's lead was but one point higher than John Major's in 1992, yet the latter was rewarded with a majority of just 21.

Apart from the low turnout in safe Labour seats, there was one other reason why Labour emerged with just six seats fewer than in 1997 even though it endured a 1.8% swing against it in votes. In the most marginal seats it was defending there was in fact a swing to Labour—thanks it seems to tactical voting by Liberal Democrats. So even though tactical switching between Labour and the Liberal Democrats was not in widespread evidence elsewhere, the relatively warm relations New Labour has forged between themselves and the Liberal Democrats again brought it a decisive benefit. In any event, Britain's electoral system is now more biased in Labour's favour than ever before. While a nine-point lead was enough to give Labour a landslide majority, the Conservatives now need an eleven-and-a-half point lead just to secure a majority of one. The current review of parliamentary boundaries will provide the Conservatives some relief but it will have little impact on most of the bias.

Labour is committed to looking once again at electoral reform for the House of Commons after 2003. But now that the system has delivered the party so many seats despite winning so few votes, it has little incentive to adopt any change. For all its radicalism, first-past-the-post is one feature of British politics

New Labour looks unlikely to alter.

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Bagehot

N(euro)sis all round

Jun 14th 2001
From The Economist print edition

A week ago William Hague was ridiculed for fussing about the euro. Now everybody is doing it

Get article background

PERPLEXING, ironic, unpredictable, unforgiving and generally pretty foul are the ways of politics. William Hague's attempt to make the euro the big issue of Britain's general election on June 7th was a calamitous misjudgment. Wrong subject, wrong moment to talk about it, was the near-unanimous verdict of pundits and voters alike. One short political week later, but with the habitually premature Mr Hague having now volunteered himself at 40 for the rubbish bin of history, the big issue of British politics for both main parties is indeed the euro.

In the case of the Tories, it is Mr Hague's going that has propelled the euro to the top of the agenda, where the poor man had wanted it a week ago. It was not in truth the right issue for the general election, because voters had a promise from Tony Blair that a Labour government would hold a referendum before joining the single currency. It is the right issue in the election of the next Conservative leader, because nobody can unite what is left of the once-great party without finding some way to bridge its internal differences on Europe.

Michael Portillo, the front-runner and first of the contenders to step into the open, said this week that this job of internal healing would be his first priority. But he has two problems. One is Kenneth Clarke. Mr Portillo could pose far more credibly as the unity candidate if he had the support of the former chancellor, who leads both the party's left wing and its remaining band of europhiles. The two men have been talking, but, as of midweek, to no avail. This is because there are limits to the sort of deal Mr Portillo can offer Mr Clarke.

As a long-time disbeliever in monetary union, Mr Portillo cannot turn on a penny and still claim to be a man of conviction. Nor would this make tactical sense. Hatred—it is not too strong a word—of the euro and the EU is rife among both Conservative MPs and grassroots party members, the two groups that will vote in turn on who is to become the new leader. And although Mr Portillo has many supporters in Parliament, including most of what was Mr Hague's shadow cabinet, he is less admired lower down in the party. He will find it hard enough to persuade the old dears and dragons in the local Tory clubs to swallow his gay past and new gospel of touchy-feely tolerance without asking them to betray their beloved pound as well.

All that Mr Portillo can really offer the europhiles is a softer tone. In declaring his candidacy, he talked of the need for Conservatives to be "internationalist" in outlook, and to co-operate with and learn from Britain's neighbours. At a stretch, he could even give Mr Clarke a job, though this requires a more delicate calculation. What if Mr Clarke demanded both a big job in the shadow cabinet and a licence to campaign in any euro-referendum in favour of joining? Besides, Mr Clarke might run for the leadership himself, not necessarily because he expected to win but to strengthen his bargaining hand for later.

The further Mr Portillo leans to the left, the more he exposes his right

Mr Portillo's second problem is that the further he leans to the left, the more he exposes his right. The main threats there are Ann Widdecombe, shadow home secretary, and Iain Duncan-Smith, shadow defence secretary. Ms Widdecombe made herself the darling of Conservatism's grassroots by promising beastly treatment of asylum-seekers, but lost ground by voting for a ban on foxhunting. She looks so odd and sounds so shrill that many of her parliamentary colleagues think she would make the party terminally unelectable. Mr Duncan-Smith, a sharp yet kindly former soldier, is a bigger threat. He appeals not only to party bigots such as Lord Tebbit, who prefer what they call a "normal" candidate with children to the once-gay Mr Portillo, but to unbending europhobes of the Thatcherite school, who detect in Mr Portillo's altered tones a suspicious whiff of garlic and defeatism. Mr Duncan-Smith is close to the camp that would welcome a total British withdrawal from the EU.

No more Schadenfreude

Although the Conservatives' leadership contest may drag on until August, Labour cannot take the delight it once did in the self-mutilating euro-contortions of its opponents. For the government now has euro-troubles of its own. Tony Blair wanted the first week of his second term to be noted for the vim of the new team of ministers who will now—really—deliver the better public services he promised last time round. Instead, the new team delivered a more barbed version of what went before: backbiting, briefings and counter-briefings that point to a government that is at best in a dither on the euro, and may at worst be almost as divided about it as the Conservatives are.

If Mr Hague's departure ended the ceasefire he had imposed on the Conservatives, Labour's re-election has made it harder for Mr Blair to remain coy about when—and whether—he will pronounce on the famous five economic tests and call a referendum. The ambiguity that was useful to Labour before the election is now making the single currency's enthusiasts impatient. Mr Blair's cabinet dispositions are being scrutinised by the financial markets as if they were Kremlin purges. Robin Cook and Keith Vaz, euro-enthusiasts, were replaced at the Foreign Office by Jack Straw and Peter Hain, who are or once were sceptics. Does this show, the Kremlinologists ask, that the prime minister is cooling on the euro, or merely that he is recruiting more plausible salesmen for an early referendum?

Nobody can say. The only certainty is that friction persists between Gordon Brown, chancellor of the exchequer, inscrutable custodian of the five tests and presumed sceptic, and almost all of the pro-euro ministers, who may or may not include the prime minister himself. Mr Blair could stop the guessing by signalling whether and when he intends to act. But such a course is fraught with risks, not the least of which is that by resolving the issue either way he will get the Conservatives off a hook on which he would prefer by far to leave them dangling.

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Ulster

Bad for peace

Jun 14th 2001 | BELFAST
From The Economist print edition

The outcome of Ulster's election spells trouble for the peace process

THE results of the general election have not helped the cause of peace in Ulster. Unionists are frightened by the growing nationalist share of the vote and the extent of support for Sinn Fein, the IRA's political voice. Moderate republicans fear that the surge in support for the veteran hardline unionist, the Reverend Ian Paisley and his Democratic Unionist Party (DUP) makes ground for compromise harder than ever to find.

AP

Woe for Trimble

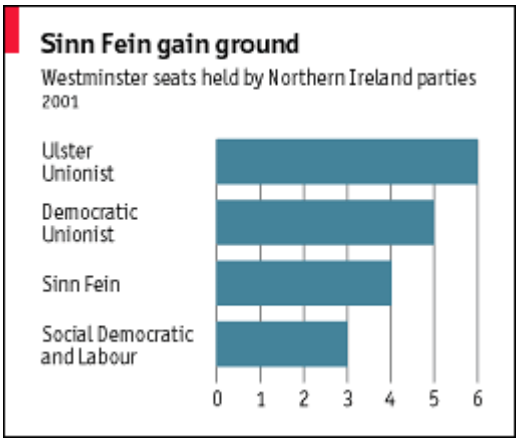
The harsher post-election climate means that David Trimble, the pragmatic leader of the Ulster Unionist (UU) party, who has headed a rickety, power-sharing coalition at Stormont since 1999, may be forced to fulfil his promise to resign by July 1st. His resignation might finally destroy the peace process.

In the run-up to the election and under pressure from more inflexible unionists, Mr Trimble said he would pull out of government with Sinn Fein's two ministers unless the IRA made moves to decommission weaponry by the end of June. The trouble is that anything republicans seem likely to offer would fail to satisfy Mr Trimble's unionist enemies.

They have already dismissed as fraudulent three inspections of arms dumps by international assessors. One of Mr Paisley's new MPs, Gregory Campbell, said that before the DUP would talk to Sinn Fein, the IRA would have to show that it had dismantled its organisation and totally disarmed.

Ulster Unionists are now down to six seats at Westminster, having lost three in the election and with their lead over Mr Paisley's party in local government cut to a slim 1.5% of the vote. Mr Paisley went into the elections with three MPs and came out with five as the second largest party. Sinn Fein beat the moderate SDLP into fourth place among the parties in terms of total votes, and took two UU seats. In local government the SDLP still leads, but by a margin of only nine seats.

One of the most telling sights of the election was that of Mr Trimble and his wife Daphne, outside the count for his Upper Bann constituency, surrounded by Paisleyites screaming "traitor", throwing punches and kicks at them. The UU leader made an angry victory speech. But he was probably less shaken by the yobbish reception than by his much reduced majority over a first-time DUP challenger.



Anti-Trimble Ulster Unionists are divided on how to proceed. DUP success is all the more galling because the party has kept its own two ministers in the power-sharing executive while continuing to damn Mr Trimble for agreeing to set up the structure. The former UU chief whip, the Reverend Martin Smyth who is MP for South Belfast, citing the results, has already said he is willing to challenge Mr Trimble's leadership at the UU's annual council meeting on June 23rd. The 38-year-old Lagan Valley MP Jeffrey Donaldson is less willing to show his hand but thought to be the more serious contender. Two other leading critics in the party and the forceful maverick Robert McCartney lost their seats, which in other circumstances would have boosted Mr Trimble.

The Ulster Unionist leader met Tony Blair this week to press home his demand that the republicans put weapons "verifiably beyond use", the euphemistically phrased promise made in various forms since the

peace process began. Mr Trimble said he was determined by the end of the month to “cause a crisis in the institutions if the agreement with regard to decommissioning has not been implemented.” Mr. Blair will be keen to persuade Sinn Fein leaders of the need for action. They have said that IRA decommissioning can be resolved, suggesting that Mr. Blair might make parallel moves on demilitarisation.

But one of the new MPs Mr Trimble brought with him to Downing Street, David Burnside, announced prior to the meeting that he believed the IRA was about to seal an arms dump with concrete. Sealing dumps has been mooted for some time. It would not do, said Mr Burnside.

Devolved government had begun to develop a sense of stability built on the flawed but durable ceasefires by mainstream paramilitary groups. The post-election mood has erased that sense. If no acceptable form of decommissioning emerges and Mr Trimble resigns, formal suspension of the institutions looks to be the government’s only choice. But neither Mr Trimble nor the SDLP are ready for renewed negotiation. The DUP’s increased mandate is for determined exclusion of Sinn Fein. The peak of the annual marching season with its freight of inter-communal tension is only weeks away. Violence may once more fill a political vacuum.

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Freight transport

Marine motorways

Jun 14th 2001 | EDINBURGH
From The Economist print edition

Put it on a ship

THE government wants more freight to be moved from lorries and congested roads on to the railways. But, despite its urging, only about 8% of British freight is carried by trains, exactly the same proportion as ten years ago. So how about trying to take it by sea?

This may not be as daft as it sounds. Next May, Superfast Ferries, a Greek shipping company, plans to start a daily roll-on, roll-off ferry route between Scotland and a Belgian or Dutch port. Until recently, it has been quicker to take Scottish goods to the continent by road and then ferry from the Humber or the Channel ports. But the Greek ships' speed of 27 knots (32mph) is a third faster than the best conventional ferries, making them an attractive option for Scottish exporters.

Alexander Panagopulos, managing director, says he is confident that the new service will succeed. From starting in 1995 with one fast ferry, which now cost £65m each, the company now has six zipping between Greece and Italy. Four more will be shipping lorries between Germany, Finland and Sweden by 2002. Cargo carriage in the Adriatic has grown by 6% a year, and passenger numbers by 4% a year, he says.

English road users will benefit from the North Sea route. About 250,000 lorry journeys between Scotland and the Continent are made every year. All, at present, go through England. The fast ferries could take, it is estimated, about a third of this traffic. The prospect is interesting enough for the government, and some shipping firms, to wonder whether fast ferry services around British coasts might take even more freight off roads.

The transport and regions department has set up a "marine motorways" study group. Academics from Napier and Heriot Watt universities are looking at four possible routes. Edgar Martin, of Napier's maritime transport group, says the initial work suggests all are feasible, but profitability has yet to be proven. At the rate England's motorways are snarling up, sending lorries to sea might be a better idea than trying to put them back on the rails.

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Urban regeneration

Grandstanding on the Tyne

Jun 14th 2001 | GATESHEAD
From The Economist print edition

In search of a new cultural reputation

SAT on the south bank of the river Tyne, Gateshead has always been the poor relation of the richer Newcastle on the other bank. Its town centre, an ugly 1960s concrete concoction, looked even worse when the Metrocentre, a modern shopping complex, was built a few miles to the west. But not everyone cheered when developers proposed rebuilding Gateshead's decrepit centre.

Film buffs, particularly fans of the cult British gangster film of the 1970s, "Get Carter", were dismayed. The centre's truly hideous multi-storey car park was the location where the anti-hero, played by Michael Caine, disposed of a local hoodlum by throwing him off the roof. "It is part of the landscape," says Chris Riley, who runs tours of the area.

Gateshead is trying hard to acquire a new reputation. It is already publicising the opening next year of the Baltic Mills, a £46m conversion of an old riverside grain store into a vast contemporary art gallery. A year later, a £62m regional music centre is due to open in the shadow of the Tyne Bridge. With two concert halls, it will be the home for the Northern Sinfonia orchestra and Folkworks, a folk music and dance company. The building, a stunning design by Norman Foster, is meant to resemble a tidal wave crashing out of Gateshead into the river below.

These two projects have given grand ideas to Tyneside's civic fathers. Newcastle and Gateshead town halls are trying against competition from other British cities to persuade the EU to designate them jointly as Europe's city of culture in 2008. The aim is clear: to make the region more known for fun than hard graft.

Daring stuff. But it may also be financially perilous. The gallery and concert halls in Gateshead are only there by courtesy of lottery subsidy. It is paying out £81m to cover three-quarters of the building costs and has contributed another £9m towards a stylish footbridge across to Newcastle's modish quayside.

Keeping things going is more difficult. Big lottery-funded projects often run into trouble when the projected visitor numbers fail to appear. The Baltic Mill hopes to lure 345,000 people in its first year, dropping off to 250,000 visits annually. Even though it won't charge entry fees except for special exhibitions, this looks like a tall order in an area where contemporary art is a new phenomenon.

Gateshead Council, however, seems determined to keep ploughing money in. It argues that culture is driving an economic renaissance in the eastern half of the borough around the quayside projects. Close by the gallery and music centre, a Hilton hotel is being built. Taylor Woodrow is about to spend £100m on building a hotel, flats, cinema and other leisure facilities.

Extravagant claims are being made for the music centre. Alan Smith, an extrovert local architect, who chairs the Baltic's fund-raising trust, asserts that the building will become as famous an architectural landmark as Sydney's opera house. Well, maybe. At least, it should make a great set for a movie.

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Wildlife

Dam builders

Jun 14th 2001 | EDINBURGH
From The Economist print edition

Ospreys, kites, beavers

FEW things are more likely to excite city slickers than unusual wildlife. So Rutland's tourism businesses cheered up this week when a pair of ospreys successfully produced a chick at their Rutland Water nest, the first for more than 150 years. Lake District hoteliers are crossing fingers that another pair of the fish-eating eagles will be equally fertile. Perhaps one answer for rural economic problems is for more creatures, beasts as well as birds, to be brought back to the countryside.

Hungry chicks

Quite apart from improving biodiversity, new birds are a big box-office draw. Around 30,000 people a year visit the Royal Society for the Protection of Birds' (RSPB) Abernethy Forest estate in Scotland, many just to see ospreys. A visitor centre near Inverness devoted to the red kite, another recently returned bird of prey, gets 25,000 people a year. The RSPB says that many people are willing to trek a long way to view the capercaillzie (a giant game bird) or white-tailed sea eagles, two other reintroduced species.

Buoyed by these successes, Scottish Natural Heritage (SNH), an environment quango, is working at bringing back the beaver, which was hunted to extinction in Britain in the 16th century. A dozen beavers are to be brought from Norway and set free in the west Highlands in 2003.

The idea is popular with most locals but not with landowners and anglers. They fear that salmon-fishing, not the money-spinner that it used to be thanks to dwindling numbers of fish, will be further disrupted by beaverish dam-building. But the environmental experts claim that the European variety of beaver does not build nearly as many dams as its energetic North American cousins. SNH plans to monitor the beavers closely. It says it will remove them if they cause too much damage. But it calculates that after five years there will be no more than 40 beavers, and says that their activities should help other local wildlife.

Should the restorationists go further? Britain's ecosystem is short of carnivores, says Stephen Harris, a zoology lecturer at Bristol University and chairman of the Mammal Society. Bringing back the lynx (last seen around 180 AD) would keep down rabbits. Restoring the wolf to Scotland (killed off in 1749) would thin out the Highlands' overlarge stock of deer. Sceptics point out that wolves might not do much for tourism if a hill-walker got eaten. But the lynx has been brought back in Switzerland without upsetting tourists or farmers.

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Opinion polls

Getting it wrong

Jun 14th 2001
From The Economist print edition

A Labour tilt

POLLSTERS are in the business of producing honest statistics. So it was something of a surprise when the pollsters' trade association claimed in a press release immediately after polling day that the polls had confounded their sceptics. For in truth the performance of the polls in the election simply served to underline the doubts about their accuracy that have never been fully dispelled ever since the industry infamously failed to anticipate the Conservatives' victory in 1992.

There were two disturbing characteristics exhibited by the polls at this election. The first was disagreement. Double-digit differences in the estimate of the Labour lead were commonplace. For example, one poll conducted by MORI over the first weekend of the campaign put Labour's lead at no less than 28% while another conducted at the same time by Rasmussen put it at just 14%. Such a gap, consistently repeated across much of the campaign, cannot be explained away by bad luck. It is the product of error. The second and more serious feature was bias. Every single one of the 29 commercial polls published during the election put Labour's lead above the nine points that eventually materialised on June 7th. On average, the final poll produced by each company overestimated Labour's lead by five points. While ICM and Rasmussen, the two polls that consistently reported the lowest leads during the campaign, produced the most accurate final polls, even they both overestimated the lead by two points.

No individual poll can be expected to be entirely accurate. But if the underlying methods of the polls are sound then some should underestimate the lead while others overestimate it. If on the other hand every single poll overestimates the lead then something is seriously wrong.

Moreover, the pro-Labour bias at this election was not an isolated incident. This is the third general election in a row at which the polls have systematically overestimated Labour's lead. The polls also overestimated Labour's strength on the occasion of the European and devolved elections in the last parliament. In short, they have probably been consistently overestimating Labour's lead for the last ten years.

Far from patting themselves on the back—or hiding behind the undoubted accuracy of the BBC and ITN exit polls—the message the pollsters should take from this election is that they need to conduct a thorough review of their methods. Otherwise, come a closer election, the industry could be heading for disaster once more.

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Saudi Arabian justice

Cruel, or just unusual?

Jun 14th 2001 | RIYADH
From The Economist print edition

A look at Saudi Arabia's Islamic laws and the judges who apply those laws

NEXT to Afghanistan, no country imposes tougher Islamic laws than Saudi Arabia. The resort to beheading, hand-chopping and whipping fuels tabloid gore and human-rights outrage. Yet, cruel as the system often is, the deeper trouble may lie less with the letter of the law than with the obtuse, opaque and clumsy ways it is applied. Inefficiency, not excess, is what is now prompting belated efforts at reform.

Most Saudis take pride in their legal system, or at least in the fact that it can claim to be purely Islamic. The kingdom is the only state to hold the Koran as its constitution, and the only one where judges are trained solely in the *sharia* or Islamic jurisprudence. These traditions, along with the 250-year-old alliance between the ruling al-Saud family and the arch-fundamentalist Wahabi sect, form the core of the Saudi sense of identity.

This is why Saudis tend to bristle at western criticism of their laws. Alarm over the recent sentencing of four Britons to be flogged for dealing in alcohol moved the head of the kingdom's Supreme Court, Sheikh Saleh al-Luhaidan, to accuse critics of trying to "undermine Islam".

Ordinary Saudis were appalled this winter, says a Riyadh businessman, not by seeing three westerners confess on television to a series of local bomb atrocities, but by the fact that they were not executed immediately, "as any Saudi would have been". When Crown Prince Abdullah, the kingdom's de facto ruler, recently cancelled a trip to Canada after charges there that one of the alleged bombers, a Canadian, had been tortured, his popularity soared at home.

A senior official explains that foreigners suffer under a basic misconception. "People confuse our human-rights record with government policy, but our laws were not instituted by the government," he says. "They were already here."

Yet it is not only infidels who complain. Even the ultra-timid Saudi press voices protest at muddled, shabby and hasty court procedure, and at the small number of judges who must handle an increasingly varied load—fewer than 700 for a country with 23m inhabitants.

In private, Saudis familiar with the courts offer sharper critiques. The main complaint is that judges, who have wide discretion in interpreting the *sharia*, are ignorant, and often contemptuous, of the modern world, issuing restrictive *fatwas* to preserve Saudi "purity". Recent examples include edicts banning the children's game Pokémon, telephones that play recorded music on hold, and the habit of sending flowers to hospital patients.

Such reactionary preoccupations may be understandable, considering that, by one estimate, 80% of the kingdom's judges come from the Qasim, a region in the deep centre of the country that is a wellhead of Wahabi extremism. Senior judges will admit only like-minded graduates of select religious institutes into what is in effect a priestly fraternity. One lawyer reckons that even a Qasimi jurist may be barred entry if he happens to have trained at Mecca, a place considered tainted by foreign influence. A judge who strays from the rigid conservatism of his elders risks being fired.

The narrow doctrinal outlook of Saudi judges explains the survival of legal tenets that most Muslims consider outmoded or misguided. Virtually nowhere else are women banned from driving cars, or obliged to secure a male guardian's permission to travel locally or be admitted to hospital. Nowhere else are the *qisas*, or retaliatory punishments allowed under Islam, applied with such punctilio: last August, an Egyptian worker's eye was surgically removed at the insistence of a man who lost the use of his own eye after the Egyptian had thrown acid in his face.

Alternative justice

Much of the Saudi public may accept such rulings as proper. Yet the government itself has long tacitly admitted the shortcomings of Saudi justice by the simple expedient of creating special tribunals to bypass *sharia* courts. Over 20 of these now adjudicate most commercial matters, from trademark infringements to labour disputes.

Without them the Saudi economy would probably come to a halt. *Sharia* jurists, for example, insist that interest is tantamount to usury, one of Islam's seven major sins. Since the courts will not enforce the payment of interest, the Saudi Monetary Authority steps in to cover defaults on interest-bearing loans. But circumventing religious strictures is not always so easy. Judges have recently blocked insurance laws (they say actuary science is akin to gambling) and progressive income tax (they say Islam enshrines the payment of one-fortieth of personal income to charity, and that other taxes are illegal).

Judges have recently blocked insurance laws and progressive income tax

Because of such obstruction, moves to reform the legal system are gaining momentum. A Code of Criminal Procedure, first introduced a decade ago but withdrawn under pressure from senior judges, is to be implemented next month. The new rules will help to ensure proper legal procedures and strengthen the rights of defendants, including the right to be represented by a lawyer. Legal practitioners worry that judges, many of whom take pride in ignoring "worldly" laws, may simply decline to apply the new code. Still, it is a good step.

Similarly, there is talk of establishing special courts to cover traffic offences. This, too, is an important step. Saudi roads are dangerous, not merely because of bad driving but because of the *sharia* courts' harsh, arbitrary assignment of liability.

More fundamental reforms will take time. The government, with its legitimacy tightly bound to its upholding of the faith, is wary. Yet there is something it could tackle urgently. Even Saudis who shrug off their judges as crusty and conservative charge the police, who apply the judges' rulings, with bumbling brutality. There is nothing in Islam to excuse this.

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Israeli-Palestinian ceasefire

A hard plan for Arafat to sell

Jun 14th 2001 | JERUSALEM
From The Economist print edition

Will the CIA's working plan for ending Israeli-Palestinian violence work?

NOW that Yasser Arafat has joined Ariel Sharon in reluctantly, and at the last minute, agreeing to the ceasefire brokered by George Tenet, the director of the CIA, a formal truce has replaced the patchy, unilateral Israeli-Palestinian ceasefires that have sort-of prevailed over the past week or two. But the new "workplan" remains precarious; it is already subject to conflicting interpretations. Although it says broadly what both sides should do to re-establish security, the first immediate step, as Israel has always insisted, is the reining in of violence. When this is established, other timetables will be set. Thus the onus is on Mr Arafat to deliver first—which makes it extremely hard for him to sell the deal to his people.

AP

A blockage to peace

An unconditional ceasefire was the first of several steps, both military and political, recommended last month by the committee headed by ex-Senator George Mitchell, and accepted by both sides. But even in this first stage of the plan, the devil is in the details, and in the timetable.

Both sides are instructed to stop all violent activities (examples in the past week include the Palestinian killing of a Greek monk, presumably by mistake, and the Israeli killing, also by mistake, of three Palestinian women who were hit by fragmentation shells from an Israeli tank). In addition, the Palestinians are comprehensively called on to arrest and imprison all "terrorists". Both sides, but this applies particularly to the Palestinians, are told to confiscate all illegal weapons and to end incitement to violence. The deal calls for buffer zones to be established round flash points—which, since these are all in occupied territory, the Palestinians interpret as further land grabs.

The Israelis, to show willing, have already pulled back some tanks, and removed some road-blocks. But the deal gives no dates for the full withdrawal of Israeli forces to the positions they held before the *intifada* broke out on September 28th, or for ending the blockade that has cut the West Bank into eight segments and Gaza into four. It says merely that, in a week's time, the two sides should start forging agreed timetables for these developments to happen. The Palestinians object to this, understanding that the Israelis will insist on a non-violent period before they withdraw or end the closures.

Even worse, from the Palestinian point of view, is that Mr Tenet's plan carries no mention of the political recommendations in the Mitchell report, above all the freeze on Jewish settlement-building. It is believed that Israel is looking to a six-week "cooling-off" period, during which confidence-building measures could begin to be introduced. The Palestinians argue that all this appears to go back to the days when any progress on the Oslo peace agreement hinged on Israel's view of how far the Palestinian Authority was co-operating to protect Israeli security. After an *intifada* that has cost nearly 500 Palestinian lives (and over 100 Israeli ones), the Palestinians are not ready for such a return.

On June 13th, even as Mr Arafat gave his conditional yes to Mr Tenet, thousands of Palestinians demonstrated against the ceasefire in Ramallah and Gaza city. The militant Islamist movements, Hamas and Islamic Jihad, had already warned Mr Arafat that, should he "again become an American agent" and arrest their people, they would exact their revenge in Israel.

A recent poll commissioned by the West Bank's Birzeit University reveals how hardened Palestinian attitudes have become. Some 78% of those asked said they wanted the *intifada* to continue, come what may; 74% supported the suicide operations inside Israel. Even more worrying for Mr Arafat, the poll showed that, for the first time, combined support for Hamas and Islamic Jihad outstripped support for his own Fatah movement. In such a climate it will be hard for Mr Arafat to push through the ceasefire, especially the arrests, which he insists should be preventive, not "retroactive". He risks being depicted by his people as the CIA's man, and Mr Sharon's protector.

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Sharks under threat

Predators into soup

Jun 14th 2001 | BIJAGOS ARCHIPELAGO
From The Economist print edition

Eastern promise is doing away with West Africa's sharks

TO THE people of the Bijagos archipelago, the shark is sacred. In initiation ceremonies young men from these islands off the coast of Guinea-Bissau must spear a shark and present the liver to their elders. But can this ancient ceremony survive the economic fact that a bowl of shark's fin soup can cost $150 in the Far East?

In the archipelago, and all along West Africa's coast, sharks are being "finned" to death. Fishermen can earn $50-80 a kilo for sharks' fins, far more than from ordinary fish. By the time they reach the Far East, they could be worth $500 a kilo or more, valuable as aphrodisiacs as well as for gastronomy.

The high demand is devastating shark populations in West Africa and elsewhere. Most fish, vulnerable to being eaten by bigger fish, protect their species by spawning millions of eggs. But the shark has no predator but man, and gives birth to just a handful of young. Since female sharks are often caught when pregnant, the result has been predictably disastrous. Shark-like sawfish, which are also "finned", are already virtually extinct off the Bijagos islands, and guitarfish are under threat.

In some parts of West Africa, when sharks and other similar fish have been finned, the rest of the flesh is often dried, salted and exported to places like Ghana, where there is a demand for it. Dried shark is used much as a stock cube would be elsewhere. But in the Bijagos islands, where traders are uninterested in exporting dried shark, carcasses are often left to rot on the beach.

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Sanctions on Iraq

The council, its list and its music

Jun 14th 2001
From The Economist print edition

The UN's controversial debate on changing Iraqi sanctions

THE UN Security Council has given itself until the beginning of July to decide what should and should not be exported to Iraq under new sanctions arrangements. America and Britain, the sponsors of these proposed sanctions, wanted them to come into effect on June 2nd, at the end of the old oil-for-food formula's last six-monthly period. But they failed to bring the council into line in time, so the old formula, which allows Iraq to buy only humanitarian goods, was renewed for a month. This abbreviated renewal led the Iraq government, which demands an end to all sanctions but particularly detests the American-British proposals, to halt its oil exports amid talk of yet another "confrontation".

Reuters

Waiting to rejoin the modern world

The New York debate is not over the principle of the new sanctions: America and Britain have already won that argument. The sanctions are called "smart" because the idea behind them is to make it easier for Iraq to import the things its people need, and harder for its government to smuggle in the things that most of the rest of the world does not want it to have. This is fine in theory but hard in practice, since what the Iraqi people most need, no less than the food and medicine they are already getting, are the tools to lift their country out of the stone-age to which it has been banished by 11 years of sanctions. And most of these tools come into the tricky dual-use category of goods that could, conceivably, be dangerous.

Hence the dispute over a list of things that will not be exactly banned but will be subject to review by UN monitoring committees. America and Britain propose a list that is as wide as it is long, drawing suspected items from a previous UN list and from an amplified form of the Wassenaar Arrangement (an export-control instrument, supported by 33 countries, including Russia, which succeeded the cold-war Cocom mechanism for preventing the export of sensitive stuff to communist countries).

France, which took a lead in the early days of the council's discussions, seems to have largely shrugged off the whole intractable business. But Russia is still arguing hard to have the list narrowed, and made as specific as possible. The debate became so tense at one point that the British delegate tried to lighten the atmosphere by introducing a cheerful five-minute musical interlude—a diversion that was stopped this week when the Tunisian delegate objected to its lack of seriousness.

If the sprawling American list remains as it is, and if the review committee says no to the numerous categories on it, Iraq will have little chance of rebuilding its collapsed infrastructure, and its people will remain beggared. The difference between the new scheme, which is meant to allow Iraq to import everything that is not dangerous, and the old one, which allowed imports of only obviously harmless stuff, would disappear. The public-relations exercise behind the proposals, whereby the blame for Iraqi suffering is meant to be shifted from sanctions to Saddam Hussein's regime, would be unconvincing.

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West African fish

Too many boats for too few fish

Jun 14th 2001 | HANN PLAGE
From The Economist print edition

The European Union's greed for West Africa's fish

BACK in 1968, five fishing boats operated off Hann Plage, near Dakar, the capital of Senegal. Three still used oars, two had motors. Now the sea is ploughed by over 1,000 motorised pirogues, the descendants of the old African fishing canoes. But whereas in 1968 it took half an hour to sail from the beach to the fish, today it takes over four hours, and the fishermen catch only a fraction of what they used to scoop from the ocean.

Driven by poverty and drought, West Africans have been migrating to their coast over the past 25 years. But there they face intense competition from the outside world, particularly Europe. Negotiators from the already overfished European Union—which this week proposed a 50% cut in cod and hake catches in the North Sea—are currently trying to secure continued access for their fleets in West African waters.

The EU has just struck new deals with Guinea-Bissau and Cape Verde, and is seeking them with Senegal and Mauritania. Its old agreement with Mauritania lapses next month; its one with Senegal lapsed on April 30th. All these West African countries desperately need the money from fishing licences, but they also need to safeguard their fish stocks. Over half of Mauritania's foreign exchange comes from selling fish and fishing licences. In Guinea-Bissau, one of the world's poorest countries, revenue from fishing licences is believed to be worth 40% of government income. Its latest deal will bring it *euro*51m ($43.3m) over the next five years. Senegal has earned *euro*48m in the past four years.

According to Gregor Kreuzhuber, the European Commission's fisheries spokesman, the EU's subsidised fishing fleet has 40% more boats than it needs. And since December 1999, it has been excluded from the rich fishing grounds off Morocco. The previous four-year deal with Morocco had netted the kingdom *euro*500m but the two sides have failed to strike a new accord.

Claude Martin, the director-general of the World Wide Fund for Nature, an environmental pressure-group, recently attacked the European Commission for knowing "first-hand the devastating effect ill-managed fisheries have had in its own waters", and now exporting "this unsustainable fishing practice to threatened coastal states in West Africa". Mr Kreuzhuber insists that fishing in third countries is not unethical: "the point is to make sure it is done in a proper way."

But even when a deal is "proper", it is hard to enforce. Poorly paid government monitors on foreign fishing boats in Senegalese waters are bribed by the ships' captains to certify that their catches conform to the rules. According to Adelino Tchuda, until recently Guinea-Bissau's minister of natural resources, "We don't have the capability to control anything. We don't have a navy, or any aircraft." Mauritania has both navy and aircraft, plus radars paid for by the EU, but, even so, officials believe that foreign ships regularly filch one-third more fish than they are supposed to.

Nor is it just the EU that is after West Africa's fish. The Japanese, Koreans, Russians and Chinese are also there. West Africa's own small industrial fleets, plus thousands of pirogues, are all chasing the same fish. Indeed, stocks off Dakar have collapsed to such an extent that, in desperation, the government has begun tipping old cars into the sea to create artificial reefs in a bid to attract the fish back.

According to the UN's Food and Agriculture Organisation, what is happening in the waters off West Africa is happening across the world. In a recent report it noted that up to 10% of the world's marine fish populations were depleted or recovering from depletion, up to 18% were overexploited and up to 50% were being fished to the limit. But the demand, and search, for fish continues to expand.

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Biological weapons

Bugs in the system

Jun 14th 2001
From The Economist print edition

The difficulties in strengthening the Biological Weapons Convention

THESE weapons make even seasoned generals quake in their boots. Colin Powell, commander of the forces that pushed Iraq out of Kuwait in the Gulf war and now America's secretary of state, once admitted that, as a soldier, biological weapons scared him "even more than tactical nuclear weapons". A dozen or so countries are suspected of dabbling in biological black arts. Scores more would have the expertise to do so if they chose. And though efforts are under way to shore up the complete ban on such weapons written into the 1972 Biological and Toxin Weapons Convention (BWC), advancing science, together with diplomatic differences over a new "compliance" protocol for the BWC, is threatening to make it even harder than before to uphold the ban.

Illegal and lethal

Threat	Mortality rate	Potential epidemic spread
Bacteria		
Anthrax	High	Low
Plague	Variable	High
Tularemia	30%	Low
Viruses		
Smallpox	35%	High
Ebola	High	Possible
Toxins		
Botulinum	65%	None
Ricin	High	None

Sources: DOD; Stimson Centre; *Arms Control Reporter*

Several years ago plans to destroy the remaining legal stocks of the virus that causes smallpox—a disease supposedly now eradicated—were dropped on advice from America's intelligence services, among others, that North Korea and other countries were secretly experimenting with the stuff. Others suspected of illegally developing biological weapons include Egypt, Iraq, Iran, Libya, Pakistan and Syria (the only one in this group that has not ratified the BWC). There are concerns about Russia, China and Taiwan.

The effort to bolt some monitoring provisions on to the BWC got a big push after Russia, one of its depository powers, admitted in the early 1990s that the Soviet Union had built up a huge biological-weapons programme. International inspectors then concluded the same thing about Iraq. The sense of urgency is now heightened by fears that scientific advances in the treatment of diseases could eventually be misused to attack particular ethnic or age groups. This would remove one of the biggest deterrents to the use of biological weapons: their unpredictable consequences.

Yet talks in Geneva on a draft protocol to help countries show they are keeping the BWC's rules and to help show up potential offenders are stalled. Iran leads a group of countries that wants western governments to ease tough controls on trade in biological substances. This proposal is a non-starter. Meanwhile America in particular worries both that industrial inspections may compromise valuable commercial information and that inspectors will sometimes have too few powers to pick up signs of wrong-doing. A recent report by the Stimson Centre in Washington concludes that the business concerns are overdone, while the inspection regime as now proposed is indeed too weak to help uphold the ban. An American veto, or demand for a delay to fix the inspection rules, others argue, would put the talks at risk. Either way, the November deadline for a finished protocol looks optimistic.

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The new wealth of nations

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The world is getting both wealthier and less equal. Whether that is a good thing is increasingly up to the rich, says Matthew Bishop

THE past decade was probably the most exuberant period of wealth creation in human history. It also produced an unprecedented number of wealthy people. Despite the recent disappearance of some well-known dotcom tycoons, the count of millionaires and billionaires still went up last year. The world now has 7.2m people with investable assets of at least $1m, up from 5.2m in 1997. Those 7.2m dollar millionaires control about a third of the world's wealth. According to *Forbes* magazine's "rich list", there are also 425 billionaires, 274 of them in America alone.

Why was so much new wealth created in the 1990s? How did so much of it end up in the hands of the rich? And what are the economic, social and political implications of wealth creation when it goes hand in hand with rising inequality? This survey will consider these and other questions facing the wealthy, particularly the new rich, but will assume that they will have little difficulty finding ways of spending their money. Wilfred Beckerman, an Oxford economist, surely has it wrong when he says that "The problem of creating sufficient wants...to absorb productive capacity may become chronic in the not too distant future." Look no further than the imitation Japanese palace being built by Larry Ellison, the billionaire boss of Oracle, an IT company, or the state-of-the-art armoured vehicles that are all the rage amongst the rich of Moscow and Sao Paolo, to be reassured that the supply of wants is infinite. The recent $20m trip on a Russian rocket taken by Dennis Tito, a rich American with a taste for space tourism, is unlikely to prove the final frontier.

But what exactly does it take to be rich nowadays? As Bradford De Long, an economist, writes in his forthcoming "History of the 20th Century Economy: Slouching Towards Utopia", most Americans today enjoy standards of material comfort that "were beyond the reach of even the richest of previous centuries. Even lower-middle-class households in relatively poor countries have today material standards of living that would make them, in many respects, the envy of the powerful and lordly of past centuries."

Common-or-garden millionaires

Equally, millionaires are not what they used to be. In industrial countries, almost anybody prepared to work hard, save diligently and live like Scrooge can become one. In 1956, when Cole Porter launched his song, "Who wants to be a millionaire?", it carried connotations of flashy flunkeys, a marble swimming pool and a country estate. Today, $1m would not buy you much of a house in the better parts of New York, San Francisco, London or Tokyo. "The millionaire has become common in numbers, common in the source of wealth, common in the usage of bygone snobberies in social origin, common in the continued narrowing of the gap between his fortune and that of the normally affluent middle class," notes Robert Heller, an author.

Having investable assets in the $250,000-5m range simply makes you one of the "mass affluent", as the financial-services industry now calls them. To be truly rich, you need quite a bit more than that. Silicon Valley has a useful, if gratuitously rude, phrase for the sort of money that will free you from ever having to take a job again: "Fuck-you money". This is currently reckoned to be around $10m, enough to generate an annual income of around $500,000. Above $100m, you are one of the super-rich, able to meet any conceivable need that you (or your family) might have in your lifetime. Your main worries will be about what will happen to your money when you die.

For richer, for poorer

“Riches, in spite of the most violent regulations of law to prevent their dissipation, very seldom remain long in the same family,” noted Adam Smith 225 years ago in “The Wealth of Nations”. The rich man, he suggested, “frequently has no bounds to his expense, because he frequently has no bounds to his vanity or to his affection for his own person.” To this day it remains exceptional for families to retain great wealth for more than three generations, if not always for the reason Smith suggested.

Will today’s new rich once again dissipate their wealth?

Will today’s new rich once again dissipate their wealth? The temptation to spend may be as strong as ever, but the opportunities for conserving, or even increasing, wealth through astute investment strategies have multiplied. The rich can invest in hedge funds to minimise their exposure to a sharp decline in the stockmarket; they can earn higher returns on their money by investing in venture capital and private equity funds, which are not available to the less well-off; and they can minimise their tax liability by using offshore financial centres, carefully designed trusts or special insurance policies.

“Getting this right is a huge challenge for the new rich, because the complexity of wealth management increases geometrically as they get richer,” says Maria Elena Lagomasino, head of J.P. Morgan’s private bank. But they can also buy better wealth-management advice and administration than ever before, though choosing the right adviser requires great care.

“Who is rich?”, asked Benjamin Franklin, one of the wealthiest of America’s founding fathers. “He who is content. Who is that? Nobody.” Money does not gurarantee happiness, and the rich have their share of troubles, as well as some extra ones that arise directly from their wealth—though that is not to suggest for a moment that they would rather not be wealthy, nor that they deserve any special sympathy. The Silicon Valley affliction known as “affluenza” or “sudden-wealth syndrome” has been widely reported. Rich people of all kinds are increasingly worried that their wealth will demotivate their children and make them selfish and unappreciative of the value of money.

In a famous essay entitled “Wealth”, published in 1889, Andrew Carnegie, then one of America’s richest men, claimed that “The problem of our age is the proper administration of wealth, so that the ties of brotherhood may still bind together the rich and poor in harmonious relationship.” Carnegie believed that the inequality between rich and poor resulted from the pursuit of maximum economic efficiency. In a free-market system, winners did very well and the rest did not. As this generated more wealth than any alternative system, “much better this great irregularity than universal squalor.” However, to prevent the rise of rival philosophies such as socialism, the accumulators of great wealth should use it “for the common good” by spending it “for public purposes, from which the masses reap the principal benefit.” He also argued that wealthy parents should not leave much to their children, and that the state should impose death duties in “condemnation of the selfish millionaire’s unworthy life”.

Does any of this still hold true more than a century later? Broadly speaking, in the developed world the recent growth in inequality does reflect greater economic efficiency, though not a perfect meritocracy. Bill Gates, Larry Ellison, George Soros and Warren Buffett have joined the ranks of the world’s richest men on merit—which is not the same as saying they became rich by being good. And as the rich have got much richer, the large majority of people in developed countries have also got quite a bit richer. Wealth seems to be trickling down from those at the top.

Not so in some less developed corners of the world. Russia’s new rich have become wealthy as the majority of the people have got poorer. According to Hernando de Soto, a Peruvian economist and author of “The Mystery of Capital: Why Capitalism Triumphs in the West and Fails Everywhere Else”, many of the rich in the developing world have prospered through gaining favours from the state. “The rich of the West were winners in a competitive system, the rich of the developing world won a competition for political favours.” That is why the growing wealth of a developing-world elite should not be regarded as a precursor for broader prosperity on the American model, says Mr de Soto. He fears that unless capitalism is made truly meritocratic and inclusive, there may be a revolutionary backlash against it in some poorer countries.

My family all drive armoured cars. It’s no good

Certainly the public seems far more tolerant of the rich in countries where capitalism is considered to be broadly fair. In parts of the developing world, the rich constantly fear attack. “Sao Paolo has the highest number of helicopters in the world because the rich don’t feel it is safe to drive,” says Victor Siaulys, boss of Ache, a Brazilian pharmaceutical firm, and a campaigner for change. “My family all drive armoured cars. It’s no good.”

And what of Carnegie's belief that the best way to help the masses and defeat non-capitalist political and economic models is private philanthropy? In America philanthropy plays a crucial part in financing the country's hospitals, universities, libraries, museums and concert halls, whereas in Europe and Japan the rich are taxed more heavily and therefore expect such institutions and facilities to be provided by the state. In Latin America, meeting social needs has often been seen as a job for the Catholic Church.

Barring a prolonged economic crisis and stockmarket collapse, the next 20 years are likely to see a huge increase in American philanthropy. Not all of this will be worthwhile or well done. But it will engage many of America's most creative entrepreneurs in trying to meet the country's social needs. A great deal of money will go to help the less well-off, particularly in health and education. And the rich in other countries may well follow suit.

But in order to give away lots of money, would-be philanthropists first have to make it. The next section will take a closer look at how the new rich got so wealthy.

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Loaded

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How the new rich got where they are

IT WAS politics, not prurience, that inspired the publication of the modern world's first "rich list", in 1892. American protesters against protectionism argued that tariffs on many imported goods had turned some 31,000 businessmen into millionaires. To refute this claim, the publisher of the *New York Tribune*, a fervent supporter of tariffs, drew up what he reckoned was a complete list of all the millionaires in America. It ran to a mere 4,047, of whom only 1,125 had become rich in industries protected by tariffs.

In 1982, when *Forbes* magazine first published its annual list of America's 400 wealthiest families, the threshold for inclusion was a net worth of $90m. In last year's money that would have been $161m, but by that time the cut-off point had risen to $725m. Nearly three-quarters of those included in the list in 2000 were billionaires, and 18 had an estimated net worth of more than $10 billion. The richest of them all was Bill Gates, although his estimated wealth of $63 billion was well below the $85 billion it had been a year earlier, largely because of Microsoft's tumbling share price. Such dramatic swings show up the limitations of most studies of the wealthy. They generally measure investable wealth, which is highly sensitive to the ups and downs of the stock- and bond markets.

Over the past four years the number of millionaires has risen sharply in America and Europe and slightly in Asia, says the latest annual "World Wealth Report" by Merrill Lynch, an investment bank, and Cap Gemini, a consultancy (see chart 1). But the number of millionaires in other continents has remained much the same: an estimated 200,000 in each of Latin America, the Middle East and the former eastern block, and 40,000 in Africa (most of them in South Africa). Latin America accounts for only 3% of the world's millionaires, but 12% of their total assets.

Merrill Lynch-Cap Gemini found that the rich not only grew in number, but also got much richer individually. The total wealth controlled by people with assets of at least $1m nearly quadrupled between 1986 and last year, from $7.2 trillion to $27 trillion. The rich of North America (including Canada) accounted for $8.8 trillion of last year's global total, and those of Europe for $7.2 trillion. Over the past 14 years the fastest growth in assets in the hands of millionaires was in Asia, with a rise of 600%, compared with 440% in Europe, 313% in America and only 166% in Africa.

Thank the stockmarket

The recent surge in wealth is due first to the biggest ever bull market in shares, particularly in America. Movements in other sorts of wealth, such as land and property, are harder to measure, not least because its owners rarely make such information public, though its value has almost certainly gone up sharply, too. As a result, the rankings may exaggerate the rise of new compared with old wealth.

The rising stockmarket reflected not only actual increases in corporate profitability, but also the

reasonable expectation that strong profit growth would continue. The rapid spread of globalisation and market economics has been good for profits, and new technology appears to have boosted productivity. On the other hand, the ratio of share prices to corporate profits now stands well above its historic average. The broad stockmarket could still turn out to be a bubble that might burst, just as the bubble in the narrower tech sector did last year.

As it happens, last year's tech-stock meltdown had a surprisingly modest effect on the growth in wealth. The Merrill Lynch-Cap Gemini report found that the number of people with investable assets of at least $1m increased from 7m worldwide in 1999 to 7.2m in 2000. Despite anecdotal evidence to the contrary (see article), it seems that many of the dotcom wealthy held on to a decent chunk of their new riches. According to Winthrop Smith, head of private banking at Merrill Lynch, "People were more widely diversified than you might have expected."

A large amount of wealth during the 1990s, particularly in America, was created by share options held by the managers of big, established companies. Making it to the executive suite of a big American company has become a guarantee of multiple millions. If the bull market in shares becomes less rampant, future gains may be smaller. More likely, though, the staggering salary and share-options packages (often undeserved) that are the norm in America will become commonplace in the rest of the world, too.

Selling the family silver

Some of the increase in investable wealth reflects a shift of assets to the market that had previously existed in an illiquid and less measurable form. In recent years many family-owned companies have been sold, including a growing number through an initial public offering (IPO). Does this amount to wealth creation, or merely a zero-sum wealth reclassification? Probably some of each.

Liquid assets, such as publicly traded shares or the money received in a sale, can be worth a lot more than an illiquid stake in a private company. The sale of a family firm may also create wealth by enabling the resources locked up in the firm to be used more efficiently. In Latin America, in particular, many inefficient family conglomerates have been sold to multinationals and broken up. Sales of family-owned firms, and IPOs in particular, have slowed in the past year, but this has been mainly because the uncertainty in the stockmarket has made it harder for buyers and sellers to agree on price, not because the strategic case for selling has become any less strong.

Another factor that has made more people rich is the recent tendency to reward top performers in any field disproportionately well. As Robert Frank and Philip Cook point out in their book "The Winner Takes All Society", new technology, globalisation and market economics have changed the structure of many industries in such a way that their star performers now earn vastly more than the average. This has been most visible in sports and the arts, where the best can become global celebrities and sometimes earn more than those who manage and advise them, whereas average performers receive only a mediocre pay. Oprah Winfrey, who neatly combines both managing and performing in her company, Harpo Productions, is on course to become the world's first self-made billionairess.

But superstar remuneration has also become widespread in less glamorous businesses, from law to investment banking, and Mr Frank thinks this process has further to go. "The technologies that have been steering the lion's share of income and wealth gains to those atop the economic pyramid are in their infancy. The gap between top earners and everyone else will continue to grow," he says.

Wall Street bankers have been among the biggest winners of the wealth-creation boom of recent years, not least because they have earned juicy fees for repackaging wealth into investable forms. This sometimes includes their own firms—most notably Goldman Sachs, which sold itself to the public in 1999, instantly making its 189 partners worth at least $40m each. Although many of the Internet entrepreneurs who took their companies public saw their paper wealth vanish, the investment banks that underwrote the sales made a lot of money out of them.

Things will not be so easy in future, reckons John Whitehead, one of Goldman Sachs's bosses in the 1970s and 1980s. "The bubble in Internet shares created an artificial boom for Wall Street. Now Wall Street will have to get back to work and earn its living." Venture capitalists will certainly be less awash with capital than in the past two years. But Silicon Valley, which supplied many of the most lucrative IPOs of the 1990s, remains broadly optimistic, and some of its entrepreneurs seem almost relieved that the bubble has burst. "Silicon Valley existed before the runaway wealth creation of the Internet bubble," says Jim Clark, founder of Netscape. "I hope enough people have gotten burned that the bubble won't

return."

On the other hand, Bill Nguyen, who has founded several technology firms, reckons that although there "will be as much wealth created in the next five years due to technology as in the past five years, it will be much broader than Silicon Valley, and perhaps to its exclusion." This is because in future much of the wealth creation will be by established companies using technology to improve efficiency, as opposed to creating the technology itself.

At best, American share prices over the next 20 years are unlikely to rise by anything like as much as they did in the past two decades. "The value of financial assets issued and traded has grown at twice the rate of the real economy for nearly all of these 20 years and, inevitably, the growth rate must slow down to the same rate as the underlying economy itself," argues Roy Smith in "The Wealth Creators".

The last great boom for the rich ended with the stockmarket crash of 1929, the Great Depression, and the spread across the world of government policies aimed at narrowing the gap between the rich and poor. A repeat of this less-than-winning combination is unlikely. So will wealth go on being created as rapidly as it has done in recent years?

For what it is worth, the Merrill Lynch-Cap Gemini study forecasts that the wealth controlled by millionaires will increase by 8% a year to 2005, reaching $40 trillion. Over the same period, the Boston Consulting Group expects total investable wealth (everybody's, not just millionaires') to grow to $88 trillion, from $58 trillion now, and reckons that the assets of the wealthiest group will grow by 10% a year. But perhaps they are being too sanguine.

Death and taxes

In much of the world, governments over the past 20 years have moved away from the punitive marginal tax rates with which they used to hit the rich. The idea was to make hard work more worthwhile. The coincidence of lower tax rates with rising wealth suggests that the ploy was successful, but economists struggle to provide proof of a causal link. In America, according to Joel Slemrod of the University of Michigan, "It is difficult to link the recent surge in incomes at the top to tax policy."

Perhaps the tax cuts had a muted effect simply because the rich were already keeping their tax bills down through a mixture of trusts, charities, insurance and offshore private banks. At any rate, few economists think that further tax reductions would do much to boost wealth creation. The rich themselves, at least in America and Britain, seem much less exercised about taxes than in the 1980s, when tax cuts were crucial to the election success of both Ronald Reagan and Margaret Thatcher. President Bush's $1.3 trillion package of tax cuts, which will benefit mainly the rich, has actually been opposed by a group of billionaires. They argue their case on their own website.

The other certainty besides taxes is death—and the grim reaper is bound to create plenty of new wealthy people as the old ones drop off the vine. A large chunk of the wealth created in the past 50 years is likely to be passed on in the next few decades. But until that happens, what can the new rich do to make sure that they hold on to their wealth?

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Easy.com easy.gone

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But it was great while it lasted

WHAT the markets give, they can quickly take away. The bursting of the dotcom bubble made this painfully clear, and Jay Walker was exhibit number one. When early this year it was reported that building work had stopped on the mansion of the founder of Priceline, a once-hot Internet stock, he attracted comparisons to another Jay, Scott FitzGerald's Great Gatsby, an earlier symbol of wealth's ephemeral quality. In 1999, *Forbes* magazine had ranked Mr Walker as the 53rd richest American, with an estimated net worth of $4.1 billion. This year, he was a long way off the list.

At least Mr Walker sold a chunk of his Priceline shares before they hit rock bottom. So did many of the other well-known dotcommers, but very few got out anywhere near the top. Some of them were locked into their company's shares by IPO rules or because options had not vested. Investment banks were reluctant to provide true hedging of dotcom shares held by corporate insiders, though they sometimes made loans against them—often to the later regret of the borrowers. Some holders of options exercised them but did not sell their shares, and now find themselves with hefty taxes to pay on wealth that has vanished.

But many dotcommers declined to sell because they truly believed that their shares would soar even higher. "The fervour of the market created a false safety net," says Dean Dorman, who worked for Chemdex (later called Ventro), a spectacular B2B burn-out, whose share price plunged from $239 in February 2000 to 37 cents in April 2001. "People felt they were a diamond in the rough when in fact they were just another pretty smart recent business-school graduate." Some of his 500 colleagues took money out, but it was more a matter of luck than superior insight. "Those who made $2m-10m are pretty damn happy they did, though disappointed they didn't take out more. That sort of money allows you to take a sabbatical, clear your head for a year or two."

Thousands of less-than-it-might-have-beens can still add up to a lot, however. The California State Department of Finance estimates that some $80 billion of share options were exercised in the state in 2000, accounting for a remarkable 10% of its total wages and salaries that year. That was twice as much as in 1999 and five times as much as in 1998.

Alas, in the year ending last March the market value of Californian tech firms set up since 1997 declined by nearly 70%. Assuming that there will be no resetting of strike prices on the options, the decline in market value has put most unexercised options "out of the money". In effect, says Fred Furlong, an economist at the Federal Reserve Bank of San Francisco, "The potential to generate income from employee options associated with the so-called IPO tech firms in California is now nil."

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To have and to hold

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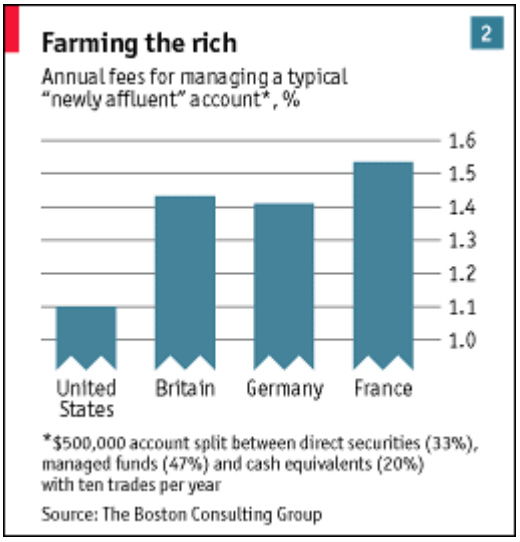
Making the money is only half the battle. Hanging on to it can be a struggle too

THE Chinese have a saying, "*Fu bu guo san dai*," or "Wealth never survives three generations." America has its own version of this saying: "From shirtsleeves to shirtsleeves in three generations." As with most old proverbs, there is a grain of truth to this—and the new rich are searching for ways to avoid history's curse.

As people get wealthier, the task of managing and retaining their riches gets increasingly complex. As well as decisions about how to invest the money, there are tax-planning issues that can make a huge difference to how much wealth survives to be passed on to the next generation.



Rich people everywhere face the same sort of wealth-management problems, but there are big regional differences in the way they invest their money. Wealthy Europeans need a more international investment strategy than Americans, who can usually find solutions within their home market. Americans find it hard to avoid domestic tax by moving money offshore because their country taxes its citizens on their global income. They concentrate on estate planning and the use of tax-exempt trusts (as the British do). Europeans often have multiple passports and tax domiciles, and their tax planning tends to be much more complex. In general, Asian tax regimes are less onerous (except in Japan), so less effort goes into avoidance.

In the past, the rich often failed to manage their wealth actively. Assets would be entrusted to a discreet and impeccably-mannered private bank, often located offshore, which would invest them securely and account for their performance perhaps once a quarter. Entrepreneurs often built great companies but neglected to build an infrastructure to manage the wealth they had created.

These days, "The very wealthy are engaged in business, not in writing poetry to each other. They want to be involved in the management of their wealth on a daily basis," says Jes Staley, head of investment management and private banking at J.P. Morgan. Indeed, some of those who got rich in the past three or four years decided to manage their wealth for themselves, trading shares via online brokerages—though the recent market meltdown has made many of them question their qualifications for the job.

The very wealthy are engaged in business, not in writing poetry to each other

Today's rich care less about the secrecy of an offshore account, because many of them have made their money through public transactions such as IPOs, selling the family firm or exercising share options, which the taxman will be aware of. Domestic political risks in many parts of the world have declined, making security less of an issue. Increasingly, the main goal of the rich everywhere is good investment performance.

There is fierce competition to provide advice and manage the wealth of the new rich. Through mergers such as Charles Schwab's with US Trust and Credit Suisse's with Donaldson Lufkin & Jenrette, private banking is consolidating both nationally and globally—although worldwide no single private bank has more than a 2-3% market share. Many banks now claim to offer a one-stop service, including asset management, tax planning and accounting. However, the quality of this integrated product varies widely.

A wealth of advisers

The new rich are less loyal to their private bank, and are more prepared than people with old money to switch to one with a better track record. The sleepy Swiss private banks are waking up to the growing threat posed by foreign competitors, especially American ones, which now account for some 25-30% of foreign money managed in Switzerland. Rich individuals already pay the same low trade-execution fees as institutional investors, but competition is also driving down the cost of private banking. However, fees in Europe remain above American levels.

Private banking is labour-intensive, with each highly paid banker dedicated to at most a handful of clients whom he knows well. A traditional Swiss private bank probably has little interest in customers with marketable assets of less than $5m. Below that level, clients are likely to be offered standardised banking and brokerage services targeted at the "mass affluent". This is a market that most financial services firms find highly attractive, because it can be run out of an existing branch network and is thus supposedly "scalable" (ie, can be cheaply expanded).

Investment banks such as Goldman Sachs and Morgan Stanley have been trying to expand their private banking businesses in the past few years, particularly by courting those whom they have helped to become rich by taking their company public. Seeing the millions of dollars raised in IPOs walk straight out of the door to a private bank was simply too much for the investment bankers to bear.

Seeing the millions raised in IPOs walk straight out of the door was simply too much for investment bankers

From the customer's point of view, whether there is much synergy between investment banking and private banking is debatable. In an institution dominated by investment bankers, the need of brokers to earn commissions by selling the bank's own investment products may be given a higher priority than offering the customer good advice. Even when banks promise "open architecture", other firms' financial products recommended by them are often dwarfed by their own brand.

The new rich in the $5m-100m category are the most vulnerable to the abuses of a commission-driven wealth manager, says Christian de Juniac of the Boston Consulting Group; particularly if they remain active in running their firm and thus have less time to keep an eye on their broker. For people with assets above $100m, advice tends to be more objective, says Mr de Juniac. Such people will typically pay wealth-management fees of over $1m a year—roughly what it would cost to poach a banker to work directly for you. Such poaching can be an effective way for wealthy families to choose between the increasingly complicated options presented to them by the private banks.

For families with $250m or more, it is common to have a "family office" with anything from five to 50 employees to oversee the financial affairs of a single family. According to the Family Office Exchange, over 3,500 American families and over 200 European ones have dedicated family offices. Over 50 institutions or families have started multi-family offices, spreading the costs of their office by sharing its services with other families.

It should come as no surprise that some of the high-tech new rich have tried to invent a better mousetrap for managing money. Jim Clark, the founder of Netscape, is behind MyCFO, launched in 1999, which claims to offer comprehensive and independent financial advice to wealthy customers. One reason for setting up the company was Mr Clark's frustration with the traditional banks. "Morgan Stanley would offer advice, but it would include mostly Morgan Stanley products. The same goes for the other banks. I wanted unbiased advice." MyCFO now has 310 clients and $44 billion under management, but doubts remain about its long-term viability. It has certainly shaken up its rivals, which now all claim to offer integrated, objective advice—though according to MyCFO, what they are really doing is "putting a coat of red paint on a Model T and calling it a Ferrari".

More eggs, more baskets

As it turns out, by far the best investment strategy in the 1990s would have been benign neglect: buy and never sell. The greatest individual fortunes were created by people with a big position in a single company's shares who held them all the way up. But in the longer term, people typically stay wealthy through diversification.

In continental Europe, in particular, the need to diversify has recently prompted a rush into equities, putting an end to the fixed-income culture that was dominant there even a decade ago. Fixed-income securities used to be regarded as wealth-preserving and tax-efficient; now the fashion has turned against

them, perhaps more than they deserve.

Some newly rich people find diversification much harder to achieve than others. Many dotcom-share-owning employees were barred from selling when the market was ripe by rules agreed on as part of the IPO process. And even when these time limits had passed, there was a danger that the market would react badly to a sale and send the firm's share price plunging. Some senior executives have minimised adverse market reaction to their share sales by placing their holdings in a trust that automatically disposes of pre-announced chunks of the shares at set dates.

Some newly rich people find diversification much harder to achieve than others

Investment banks have come up with a range of innovative ways to hedge out of a single stock exposure without actually selling. Derivatives can be used to buy protection against downside risk, and paid for by selling the right to future gains in the share price. With the share price hedged, banks will lend some of the value of the asset. Some executives who borrowed without hedging their share price have found themselves in difficulty when the share price tumbled as their bankers have made margin calls. Another hot instrument, not least thanks to its favourable tax treatment, has been the "exchange fund". This is created by selected corporate insiders from several firms pooling their holdings into a sort of mutual fund, with each receiving a proportionate ownership of all the shares in the fund.

Three strikes and you're out

Many families that own a business are looking to diversify out of the unhedged exposure that their firm represents by selling it. A number of academic studies suggest that a company should pass out of the control of the founding family within three generations; only 4% of firms survive into the ownership of the fourth generation. Many family firms in continental Europe and Latin America are now coming on the market, having been inherited by a generation much more financially sophisticated than the founders. Asians are less keen on this form of diversification, because many of them still aim to build a business dynasty.

Artists and sports stars, who account for a growing share of the new rich, find it even harder to diversify. For a start, they often receive poor financial advice. "As soon as they get millions, they are descended on by a horde of people who want to use and live off them," says Mark McCormack, boss of IMG, a firm that manages many of the world's top sports stars. Because most of them reach their peak earnings capacity early in life, they are ill-equipped to deal with their new wealth. "A 16-year-old can't easily tell a con man from an adviser who's any good. At least the dotcom whizz-kids mostly had a college education and know something. Most sports stars don't." IMG has a joint venture with Merrill Lynch to manage its clients' money, including operations in Monte Carlo that allow tax planning. Insurance is a particularly effective method for allowing its sports stars to diversify.

At least the dotcom whizz-kids mostly had a college education and know something. Most sports stars don't

The leading wealth-management firms generally have few clients from the entertainment business. According to David Pullman, a Wall Street financier, "A lot of entertainment and sports people come from poor backgrounds, and their idea of a good investment strategy is to buy five homes." Mr Pullman has helped a few rock stars to diversify by selling bonds secured against their future earnings from royalties. The first of these was for David Bowie, so they became known as Bowie Bonds (though their creator modestly refers to them as Pullman Bonds).

For the rich of every sort with liquid assets to invest, there is a growing number of more exotic ways to diversify. The most fashionable of these are "alternative investments" such as hedge funds, venture capital and other private equity. The past performance of such investments has on average been excellent, but the management fees and commissions are large, and although the minimum sums that can be invested in one of these vehicles have been coming down in recent years, in effect they are still available only to multimillionaires. These investments are also illiquid, so they are not well-suited to investors who may need cash in a hurry. And investors often overlook the need to diversify among alternative investments, and their vintage. Another risk is that many hedge funds do not actually hedge; a lot of successful hedge funds of recent years have simply borrowed to take big bets that share prices will keep rising.

In general, there is a huge divergence between the performance of the best funds, which tend to produce good results over long periods, and the majority, which often do no better than a basic equity mutual

fund, at much higher cost. But however well the constituent parts of a portfolio perform, its overall value can vary enormously depending on whether or not it is designed to minimise taxation.

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A taxing question

Jun 14th 2001
From The Economist print edition

How the rich can minimise what they pay

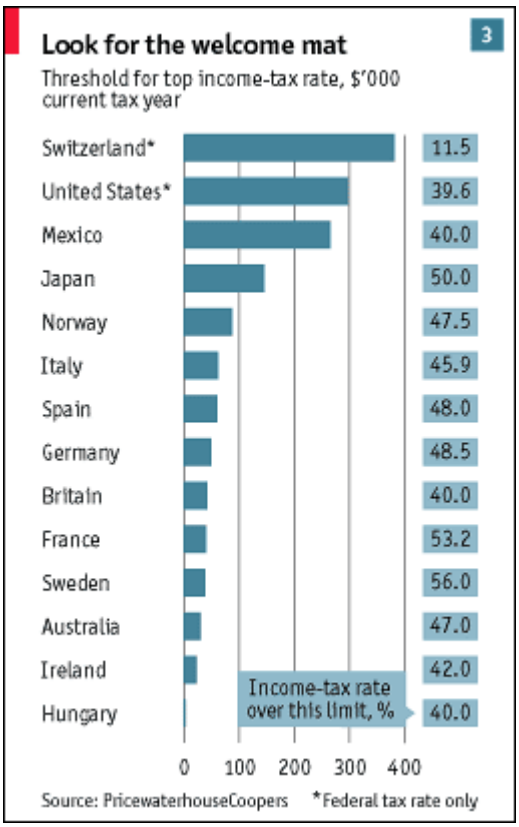
"ONLY the little people pay tax," insisted Leona Helmsley, a hotel tycoon, shortly before she was jailed for tax evasion. Some economists agree, arguing that for the rich in a global economy, paying taxes is in large part a matter of choice rather than necessity. This is an exaggeration—but for rich people who are well advised, not much of one. The sheer complexity of taxation opens up endless opportunities for them to minimise the amount they pay. As fast as governments try to close down popular methods of tax reduction, new ones are discovered.

That said, many rich people still pay a lot of tax—perhaps because they think they should contribute something, if not as much as the taxman would like them to. In Germany, for example, the 5% of people at the top of the income scale pay 40% of all income taxes collected. Even so, the rich there seem to care even more about tax efficiency than investment performance. A lot of German money finds its way to discreet Luxembourg. Likewise, many wealthy French and Spanish people are moving to London to take advantage of Britain's relatively favourable tax regime.

A big question is whether to shift assets to an offshore bank, out of reach of the local taxman. Private banking started to grow rapidly 35-40 years ago, largely because the rich wanted to move their money offshore to minimise taxes and political risk. But the advantages of being offshore have become less persuasive. In much of the world, taxes have been cut and political risk has declined. The main criterion for moving money about now is investment performance, and attractive returns are often available at home too. This is especially true of Latin America, which has recently benefited from a lot of flight capital returning home.

There is still serious political risk in the Middle East, so offshore banking remains predominant there even though domestic taxes are negligible. Middle-Eastern investors were badly advised in the 1980s and piled into dud investments. Their offshore strategies today are mostly wiser.

There are two main reasons why the new rich are likely to keep more of their wealth onshore than their predecessors. First, much of their wealth is generated by events such as IPOs, share-option exercises and sales of family firms, which are too visible to allow the money to be spirited offshore. Second, the governments of rich countries are cracking down on tax havens, particularly those in the Caribbean. Rather than be blacklisted by the OECD, places such as the Cayman Islands are reforming themselves.



Switzerland, which remains the largest offshore private banking centre, has reluctantly agreed to become less secretive in certain circumstances, and to co-operate with foreign tax authorities where appropriate. Yet Swiss banks are well aware that in their country (unlike, say, in Britain) it is not a crime knowingly to assist a customer to evade taxes. Today's law-abiding Swiss bankers may be willing to expose a big-time crook such as President Suharto of Indonesia, who shortly before being ousted is said to have shifted billions of dollars from Switzerland to more secretive Austria; but they would not abandon a mere fugitive tax-dodger such as Marc Rich. Politicians from developing countries, and rich people from Russia or China, find it increasingly difficult to open accounts with reputable international banks—though with a bit of ingenuity and will there is often a way.

As a refuge for the rich, offshore banking will survive for two main reasons, says Simon Evans of J.P. Morgan. First, offshore banks can do other things besides

providing a tax haven. For example, a lot of Taiwanese money is managed out of Singapore, Asia's main offshore financial centre, because Taiwanese cannot invest in China directly. Second, unless governments declare a general amnesty, much of the money already in offshore centres is likely to stay there, because repatriating it might incur huge back tax bills.

Till death us do part

For most rich Americans, the biggest tax-planning challenge is to avoid estate taxes—or, as those campaigning for their abolition call them, "death taxes". Federal estate tax is currently among the highest in the world, at 55% on estates exceeding $650,000. By contrast, Singapore has an estate tax of only 10%, and Australia has none at all. Italy slashed taxes on capital gains, gifts and inheritance at the start of this year to plug a constant leakage of capital offshore.

Americans get round this impost by putting their assets into a trust well before they are likely to die. Technically, by doing this they hand over control of the wealth to the trustees, who have a legal duty to administer the money in the interests of the beneficiary of the trust, be that some charitable cause or the children of the person establishing the trust. Americans also like to use life insurance as a means to avoid estate tax, which is why the insurance industry lobbied furiously against proposals to scrap the tax. Trusts are popular with wealthy Britons, too. In continental Europe, however, they are still regarded with suspicion, even though their legality has been established in several countries. There is particular resistance to handing over control of assets to a third party.

Japan also has a heavy estate tax, opposition to which is growing. Whereas the post-war generation that created much of Japan's current wealth regarded it as unpatriotic to minimise their tax liability, the next generation has no such quibbles, and has taken to using Japanese versions of Anglo-Saxon trusts. However, most Japanese wealth is tied up in property and holding companies and is not easily monetised in a tax-efficient way.

One way round an onerous domestic tax regime is to take up foreign citizenship, but it needs careful consideration. People often change citizenship only to discover unwelcome tax implications later. Over the past couple of decades many Asians have become American citizens, and thus, often unwittingly, exposed themselves to the risk of making their inheritance subject to America's worldwide tax net.

Some wealthy people still make the error of dying without a will, notes William Zabel, a lawyer, in his entertaining and practical book, "The Rich Die Richer and You Can Too". Picasso died intestate, leaving around $300m in assets; lawyers say that he was superstitious, and not making a will was "a way of avoiding death". His family spent years in the courts sorting out the mess. But then, points out Mr Zabel, "family madness" can result in lengthy legal battles even if the deceased has left a will. Ask Anna Nicole Smith, a former *Playboy* Playmate whose long-running efforts in court to get a slice of the fortune her nonagenarian billionaire husband left behind have riveted the American public.

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Rich man's burden

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From The Economist print edition

Too much money can be bad for you in all sorts of ways

AN ABUNDANCE of money is no miracle cure for all human ills, as the new rich—like each generation of the wealthy before them—are discovering. What is different this time is that there are so many more of them. As Dinesh D'Souza argues in his fascinating study of the new rich, "The Virtue of Prosperity", today millions of families "have triumphed against necessity; they are, by any historical standard, rich. So they are ready to pursue happiness, but this is where the problem begins: they don't know where to find it."

For all the existential angst that may go with being rich, there is no evidence to suggest that those with money would rather be without. Yet there are specific problems associated with being, and particularly with becoming, exceptionally wealthy. The world's leading private banks now encourage some of their clients to seek advice from psychoanalysts on their relationship with their wealth—not just in America, but also in more reticent parts of the world, including stiff-upper-lipped Britain.

There has been plenty of publicity about "sudden-wealth syndrome" (also known as "affluenza")—evidence mainly of the fact that comparatively indigent journalists like to write about the new rich having a bad time, despite their fast cars and swanky houses. Sudden-wealth syndrome was named by Stephen Goldbart and Joan Di Furia, two (inevitably) Californian psychologists, who in 1997 set up the Money, Meaning & Choices Institute (MMCI) to explore the "psychological opportunities and emotional challenges of having and inheriting money". With the popping of the dotcom bubble, they have also been quick to offer help with "sudden-loss-of-wealth syndrome".

"Twenty-nine-year-olds in Silicon Valley were finding that, suddenly, they never needed to work again, and started asking, 'what is the purpose of their wealth and life?' ", says Ms Di Furia. For many of the new rich, wealth meant a leap in social class. "They had no expectation of wealth, nor history of knowing how to live with it." The American dream has always been about the possibility of personal advancement up the social scale, but "traditionally the dream was really about going from working class to middle class, not working class to rich—and certainly not within a few years," says Mr Goldbart. "Car, house, work, the whole way of life—the new rich have often undergone a radical change in identity." Compared with the old wealthy, the new rich are "more guilt-ridden and sympathetic to the plight of ordinary Americans", says Mr Goldbart.

Though the bursting of the dotcom bubble has made some MMCI clients a lot less wealthy, most are still rich by any definition. But gone is the belief that "instant wealth automatically accompanies hard work and good ideas," says Andre Delbecq, a management professor at the University of Santa Clara Business School. "It was a wake-up call to a generation who grew up in affluence," teaching the new rich a lesson about the fragility of wealth that their parents and grandparents learned from the Great Depression and the second world war, says Mr Delbecq, who now offers a course in "spirituality and business" to Silicon Valley executives searching for a deeper meaning.

It is not only dotcom billionaires that find their new riches a mixed blessing. Sports stars and entertainers can suffer from an even greater sense of dislocation, because they are often physically removed from their familiar surroundings and spend life on the road. Marcus Camby, a basketball star at the New York Knicks, pays a salary to a childhood friend to live in his mansion and keep him company.

What now?

Sports stars also have to come to terms with their careers peaking early, and drawing to a close when most of their life is still ahead of them. According to Mr McCormack of IMG, two problems come up time and again. The first is a refusal to recognise that it is time to retire and move on to a new career. "Towards the end of their career, sports stars are more mature and receptive to advice. But it is an emotional time, and many leave it too long." A second problem is over-confidence in their ability to succeed in a second career, simply because they were great athletes. "They think because they were

good at sport, to start a restaurant or a magazine will be a piece of cake. Ninety-nine per cent of the time they get killed because of that super-confidence."

There are some parallels with the experience of family patriarchs after they have sold the family firm. In recent years many have pulled out sooner than they would have liked, partly because they were offered an attractive price, and partly because the firm was finding it increasingly difficult to survive on its own. Even though they are now flush with cash, many of these patriarchs are struggling to come to terms with losing the power and identity they got from the firm. Argentina is currently awash with wealthy 40-50-year-olds who used to run family firms and are depressed because nobody listens to them any more—and they don't want to spend their days playing polo.

A more general source of worry for the truly rich is that their wealth makes them the target of crooks and lunatics. To reduce the risk, they make growing use of private security firms, and often live in well-protected "gated communities" or secure private estates. In some countries employees of big multinational companies are in much greater danger of abduction than the local millionaires because their company will usually pay a generous ransom. A multinational typically pays around $1m-2m a year for kidnap insurance. In 1999, there were 1,789 reported abductions for ransom worldwide, up 6% on a year earlier. Over 90% took place in just ten countries, headed by Colombia, Mexico and Brazil. In most kidnap-prone countries it is mainly locals who get abducted, but in Nigeria four out of five victims were foreigners, and in South Africa one in two.

But what troubles rich people more than anything else is the effect that their wealth will have on their children. "I'm not saying, 'have sympathy for the rich', but it really hasn't been widely recognised that inheriting wealth can be a serious problem," says Alex Scott, who runs Sand Aire, the family office of the heirs (of which he is one) to the founders of Provincial, a British insurer. "The key to being a successful inheritor is not to be suppressed by the wealth, so you can go on to live a fulfilling life, exploring your own potential. But that is easier said than done."

Bad heir days

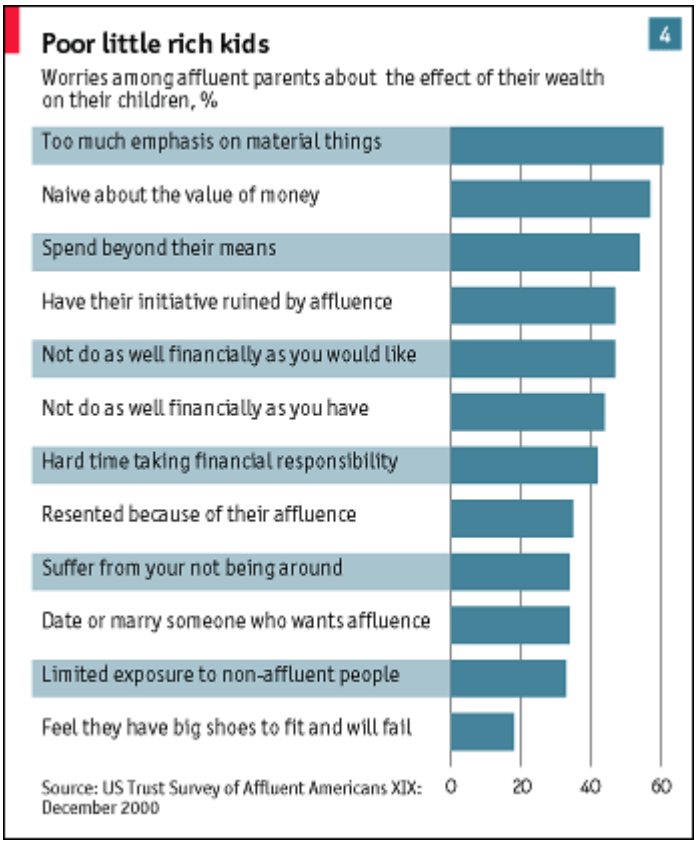
Without the need to work, wealthy people's children can become demotivated and purposeless. They can find it difficult to develop an appreciation of the value of money because they have never been short of it. They can also feel crushed by the pressure to match the achievements of the creator of the wealth they are enjoying, not least from the family itself. "Being in the shadow of a great wealth creator can be a huge burden," says Mr Scott. He himself declined to take over Provincial, which the family subsequently sold. He plans to build Sand Aire into a business that manages wealth for other families.

Teams of lawyers and psychologists often have to guide adult children who inherit a business through family minefields—who runs the firm, who gets bought out, whose spouse or child goes on the payroll. Sometimes the challenge is to talk siblings or cousins out of killing each other. Professional help should perhaps be more widely used, says Mr Scott. "Psychological counselling is probably very helpful to inheritors of wealth. American families may accept this more easily, but we as a nation are not the first to pick up the phone to our analyst."

America's new rich are more fearful than their counterparts elsewhere that their children will be deprived of the work ethic to which they themselves attribute their success. At the same time they disdain the idle rich produced by old wealth, such as the European aristocracy and the drifting trust-fund kids descended from the East Coast tycoons of the early 20th century. According to a recent survey of the richest 1% of Americans by US Trust, a private bank, around half fear that their children's initiative and independence will be undermined by having material advantages. Some 80% want their kids to find a satisfying career, and 65% want them to earn enough to support themselves entirely through their own work. But most of them accept that this is an uphill struggle. How can a child be taught that money is a scarce commodity when the most clinching reason for turning down a request, "We can't afford it", patently does not apply?

Rich American parents, it seems, try to toughen up their children by making them do household chores. According to US Trust, 99% of the poor little dears are expected to tidy their own rooms, 85% to take out the rubbish, 83% to set the table and do the dishes. Perhaps more significantly, 77% are expected to take part-time or summer jobs while at high school, and 81% to contribute to the cost of college education by working part-time. Parents are also waiting until their children are more mature before handing over wealth. US Trust found that the average age at which rich children gain control of money passed to them through a trust is 30. A current hot fad is the "incentive trust", which makes inheritance conditional on the heir behaving. The conditions can be onerous, with a "hand beyond the grave" guiding

everything from choice of university course, career and spouse to avoiding and curing substance abuse.



Most of the leading private banks offer “sons and daughters” events to educate rich kids about wealth. A growing number of family limited partnerships are being created which allow children to work alongside parents in managing the family fortune without actually getting control of the money. Such schemes provide a tax-efficient way of transferring wealth between generations, and also offer a method of stopping the family money going to an ex-spouse. Only 27% of rich parents would advise their children to get a pre-nuptial agreement, and even if they did their advice might be ignored: such unromantic agreements are rare in first marriages (though not the second time around).

Many of America’s new rich are seriously considering an extreme solution to the work-ethic problem: handing over only a little, if any, of their money to their children. But most wealthy families in other countries would consider that a counsel of despair. Much more than their American counterparts, they regard being able to pass wealth down the generations as one of the benefits of getting rich. Besides, this option is typically open only to the person who created the wealth and can do with it as he wishes. Second and later generations would find it difficult withholding money that was given to them rather than earned by them.

Bill Gates, it is said, plans to leave only $10m each to his two children, a tiny proportion of his fortune. But even that might be enough to demotivate them. For most people, it would be plenty to live on without ever doing a stroke of work. According to the US Trust survey, rich parents reckon that the motivation of an heir will start to be affected once they pass on more than about $3.4m.

The new rich might usefully learn from one of the few American family dynasties that has coped well with its fortune. According to David Rockefeller, the 86-year-old grandson of John D. Rockefeller, who made a vast amount of money in the oil business a century or so ago, “How you bring up children is crucial. If they have a sense of responsibility, you do not have to worry about how the money will affect them. My parents brought us up to know that with opportunity comes responsibility.” For the Rockefellers, one of their biggest responsibilities is philanthropy. A growing number of the new rich are hoping that this may offer a solution to their problems too.

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Giving something back

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From The Economist print edition

A golden age of philanthropy may be dawning

FOR someone who has just spent a record $62m of his own money to get elected, Jon Corzine makes a surprising observation. “The rich are getting increasingly active in philanthropy and the political world. The political side is more difficult and less important than what is going on in philanthropy.”

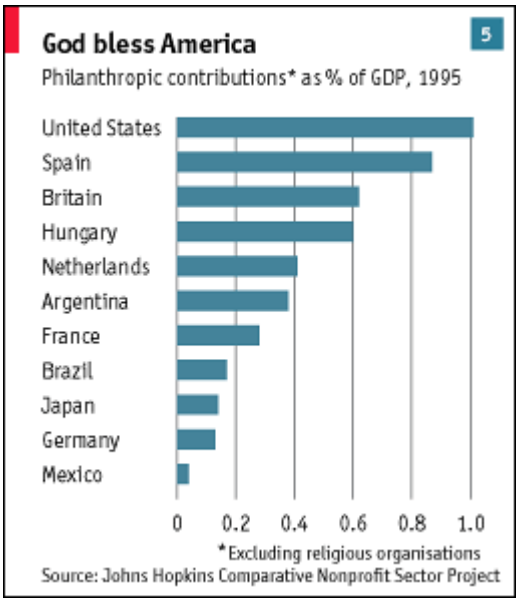
Using the fortune he made as head of Goldman Sachs to become senator for New Jersey certainly exposed Mr Corzine to the difficulties of the political side. He faced accusations of trying to buy the election, and was questioned about whether all his money was obtained from ethical activities. But he is philosophical about this sort of sniping, and reckons it is probably inevitable when a rich person runs for office. Nor is there any guarantee that spending a lot of money will bring electoral success.

Those tycoons around the world who are prominent in politics represent a wide range of opinion. On the right, there is Silvio Berlusconi, Italy’s new prime minister, who according to *Forbes* is the world’s 14th richest man, along with Christoph Blocher, a Swiss nationalist (227th); the left caucus includes David Sainsbury (109th), a minister in Britain’s Labour government, and Mr Corzine and (once-rich) Maria Cantwell in America’s Senate. Provided there is full financial disclosure, there seems no obvious reason why the rich should not be allowed to play a full part in the democratic process.

But they would get better approval ratings from a public that still generally frowns on wealth if they devoted their energies to philanthropy rather than politics. Is Mr Corzine right that philanthropy—with a few honourable exceptions—is usually a better way for the rich to use their time and money?

Philanthropy has long been a crucial part of American life, though there are signs that it is becoming increasingly important in other countries too. A century ago, Andrew Carnegie and John D. Rockefeller spent fortunes establishing libraries, museums, universities and music halls. In America, charitable giving of all sorts totalled $203 billion in 2000, around 2% of GDP (up sharply from 1995, see chart 5). In other countries the cash value of philanthropic contributions is proportionately much lower.

“Americans have a much greater tendency to think about serious philanthropy at much lower levels of wealth,” says Ms Lagomasino of J.P. Morgan private bank, which runs a global philanthropy forum where its wealthy clients can exchange ideas. Nine out of ten of the bank’s clients in America have some significant philanthropic interest. Americans seem to start giving chunks of their money away once they are worth around $20m, whereas in other countries the threshold is more like $100m.



Philanthropic giving in America is forecast to soar over the coming decades. A new study by the Boston College Social Welfare Institute forecasts that the intergenerational wealth transfer during 1998-2052 could be at least $41 trillion, of which $6 trillion might be devoted to philanthropic purposes. If average annual GDP growth turns out to be faster than the 2% assumed in the study, the figures could be larger still. Allow for the rising trend in giving by people while they are alive, and there should be enough money for good causes to achieve extensive social change.

Save as you give

The Boston study expects the rich to hand out even more generous gifts if estate taxes are phased out, as the Bush administration’s recent tax reform intends. With less tax to pay, the argument goes, the rich

will have more money to dispose of, and will split the extra between their heirs and philanthropy. “Most philanthropy is tax-motivated,” says William Zabel, a tax lawyer and writer on related matters. “The notion that charity wouldn’t be hurt if you eliminated the death tax is absurd.” Many charities agree with him, and have lobbied hard to keep estate taxes.

Giving favourable tax treatment to charitable donations is on the political agenda in many countries. Charity is one way of supplementing the services provided by the state, which are becoming ever harder to finance out of taxation. In Europe, the state’s leading role in areas such as higher education, health care and civic amenities such as museums may have discouraged private philanthropy. Tax concessions on private giving may help to change that.

The Boston study is optimistic that philanthropy will continue to grow. First, the proportion of estates left to charity is steadily rising. The share of estates of $20m or more allocated to charity increased from 34% in 1992 to 49% in 1997. Second, many interviews with donors suggest that there has been a fundamental shift in the motivation for giving. According to Paul Schervish, one of the authors of the study, the rich used to give only when they were “scolded into it—told they were not giving enough to the right causes at the right time in the right way.” Now they are increasingly giving out of inclination—“doing something they want to do, that meets the needs of others, that they can do better than commercial interests, government or existing philanthropists, that expresses gratitude for their wealth and their identification with others, and that makes them happy.” Mr Schervish thinks this shift to giving out of inclination is a result of people getting richer, and will fuel philanthropy everywhere. He sees signs of it as far afield as India, Ireland and Latin America.

Inclination, not guilt, certainly seems to be motivating Bill Gates, whose gift to charity in real terms is the biggest of all time (see article). So, too, Ted Turner, who gave $1 billion to the United Nations—though he could not resist the temptation to scold other wealthy Americans that they should give more.

But rich donors may have other motives too. Adam Siegel, head of strategic philanthropy at Hill & Knowlton, a public-relations firm, reckons that many of the new philanthropists are driven by “self-promotion, taking credit, branding yourself. They are not acting out of a sense of obligation, but rather to be a celebrity—Mr Literacy, or whatever. A lot of passion goes into it, even so.”

Cynics also say that inclination may amount to nothing more than giving to your favourite hobbies rather than tackling the basic needs of society. The arts and religion always do well. All the same, a growing number of the new rich are turning their attention to health and education. For example, the co-founder of Netscape, Jim Barksdale, is supporting basic literacy programmes for children in Mississippi.

The biggest sceptic of them all is Larry Ellison, the boss of Oracle and the world’s second-richest man. So far, he has declined to compete in largesse with Mr Gates, his arch-rival. In his view, the public’s attitude to philanthropy is “deeply bizarre...We measure philanthropy by how much money you waste. We measure the size of your donation, not results.”

Even if it is an excuse for being tight-fisted, Mr Ellison has a point

Even if it is an excuse for being tight-fisted, Mr Ellison has a point. Results matter. But the newly rich philanthropists are well aware of that. Some even call themselves “venture philanthropists” because they are trying to take an entrepreneurial, businesslike approach to their giving. They are often critical of established charities, which have struggled to win donations.

David Rockefeller thinks that rather than attacking the old foundations, the recently rich should seek their advice. “Some new philanthropists are floundering a bit, not sure how to do it. Grandfather said giving money away effectively needs as much effort and thinking as making it. It is not something people with no experience can do well without assistance.”

Philanthropy may not be able to achieve the scale of some state-financed activities, but it can engage the creativity of a country’s most successful people, rather than causing their resentment by confiscating some of their wealth in tax. Charities can take risks where governments cannot or will not. Nor should this be seen as an “either-or” choice: charities can complement and influence government policy, as shown, for example, by Michael Milken’s efforts to find a cure for prostate cancer. Mr Milken, a disgraced former junk-bond king, has become one of America’s leading philanthropists since leaving jail. And, as he has pointed out, each dollar invested in philanthropy can be leveraged by the efforts of volunteer workers.

The biggest doubt about charitable giving concerns its accountability, particularly once its founder has

died. One of America's biggest charities, the Ford Foundation, has caused much controversy by funding initiatives that Henry Ford himself would have hated. Foundations often end up in the control of professional charity workers, who can exercise considerable power, but may not be accountable to anyone. Roy Smith, author of "The Wealth Creators", fears that unless this problem is tackled, huge amounts of capital could end up being squandered by inefficiently run foundations.

Donors can help to prevent "mission creep" by defining clearly what they want their foundation to do. Unless they are as rich as Croesus, they may prefer something more targeted than the Rockefeller Foundation's mantra, which is "to promote the well-being of mankind throughout the world". More radically, they could set a time limit on the life of their foundation, requiring it to be wound up, say, 10-20 years after their death, or after the departure of the last blood relative from the board.

Going global?

Perhaps the most interesting change in approach to philanthropy—though still in its early stages— is taking place in Latin America. "There is a mind-set change from regarding poverty as a permanent aspect of civilisation," says Fernando Espuelas, the youthful boss of Star Media, a Latin American Internet content firm. His company's share price has plunged alarmingly, but he remains upbeat. "The Catholic idea that suffering is good exonerated the old wealthy from any sense of responsibility for the poor. The next generation is more sophisticated, understanding that as Latin America moves beyond military dictators, the key to social stability is a more equal distribution of wealth."

Latin Americans tend to hand out charitable donations through companies, rather than in a personal capacity, because the tax system does not encourage philanthropy. The Star Media Foundation, created two years ago, aims to narrow the digital divide by providing education and technological training for the have-nots. If it succeeds in its aim, then Star Media benefits too. This strikes Mr Espuelas as a win-win situation. "Our goal is to create conditions in which it is possible to be profitable. Lifting people out of poverty is good for society, and so is having profitable companies."

From almost nothing, philanthropy is increasing rapidly in Brazil, led by big business, says Victor Siaulys, boss of Ache, a drugs firm. Multinationals operating in Brazil have put a lot of effort into improving education and childcare, shaming domestic firms into following suit, mainly by trying to stop children working. This is an area in which the government has failed to deliver. "We are in the most tragic situation in the world in terms of inequality," says Mr Siaulys. "Philanthropy is the way to invest in a better place to live."

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Saint Bill

Jun 14th 2001
From The Economist print edition

How to give away riches beyonds the dreams of avarice

"PEOPLE would see me at cocktail parties and wonder if I was going to come up and talk to them about tuberculosis. I was the TB guy." Listening to Bill Gates holding forth about vaccinating the world's poor, it soon becomes clear that he is not doing this merely to polish an image tarnished by the antitrust action against his company, Microsoft. He could have done that with a lot less money.

The $21 billion with which he endowed the Bill and Melinda Gates Foundation makes it the world's richest charity, and the biggest philanthropic give-away ever. Developed countries may be worrying about the side-effects of this or that vaccine, but in the developing world there is no doubt that Mr Gates can improve the lives of literally billions of people.

Time was when Mr Gates was criticised for a lack of charity, despite endowing two smaller foundations, but he says he has known since his early 30s that he wanted to put the bulk of his resources into charitable activity. He "knew I'd been fortunate, and wanted to give something back—not lucky in the sense that I found the code sitting on a desk, but in terms of the circumstances, the time and country I was born in."

But he had not expected to do so much so soon. "I used to have the notion that I would wait until my 50s and 60s to put substantial resources into the foundation. I wondered if there was really something where I could make an impact. Then I saw a cause I believed in. Seeing how urgent the needs are changed my time line."

His eyes were opened when he read a World Bank report on investing in health (which should encourage bureaucrats everywhere: their work can make a difference after all). He saw the opportunity to use his vast wealth to correct a huge "market failure on the research side. A lot of diseases exist primarily in places where there is no prospect of a viable drugs market because of a lack of resources." The world's governments were unwilling to bear the risk of investing in research that might not pay off for 20 years, if at all. And health issues are a political minefield that can be more easily negotiated by a private foundation.

Does he think other rich people should emulate his philanthropy? "I love Ted Turner for saying there should be more of it. But you can't shame people into being more philanthropic. They have to come to it with their own enthusiasm." Still, he notes that most philanthropists, even the newer ones, are a generation older than he is, and thinks there remain plenty of causes where the younger new rich could make a big impact. He is "happy to talk about this to any of the new rich guys in confidence". Just ask him to a cocktail party.

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Don’t let’s be beastly to the rich

Jun 14th 2001
From The Economist print edition

The wealthy are increasingly a force for good

FOR most of history, the attitude of the majority of the human race to the rich minority ranged from grudging acceptance to fear and loathing, mostly with good reason. As democracy spread, these feelings lingered, giving rise to payback policies such as punitively high marginal tax rates and hefty estate taxes on the wealthy. More recently, governments have become more aware that squeezing the rich too much is in nobody’s interest because it risks putting off society’s most effective wealth-creators. Yet there is still no broad acceptance that those wealth-creators might be making a big contribution to the common good. That is a pity.

More than a century ago, Thorstein Veblen argued in “The Theory of the Leisure Class” that “The accumulation of wealth at the upper end of the pecuniary scale implies privation at the other end.” This is still true in some of the world’s poorer countries where capitalism lacks the underpinning of the rule of law and effective property rights for all. But in prosperous, democratic countries it is clearly not so. True, these countries are not perfectly meritocratic, and may become less so as huge fortunes pass from the creators to their heirs. Inequality has also increased as the rich have got richer—but this is because income and wealth at the top have grown even faster than for the bulk of the population.

At the same time, though, the balance of evidence suggests that incomes at the bottom, too, have been rising noticeably. The rich may have helped themselves to the largest slice, but the whole economic cake has got so much bigger that most people have more on their plates than they did 20 years ago.

Even in the current economic slowdown, the American model of wealth creation is widely admired around the world; less so the wealthy people who have prospered thanks to its application over the past couple of decades. Yet a remarkable change is taking place among America’s rich that their counterparts elsewhere should be encouraged to emulate. A growing number of Americans who have become wealthy beyond their wildest dreams are looking for ways to put their fortunes to work for the common good—just as Andrew Carnegie advised more than a century ago.

Follow the American way

Clearly there are plenty of rich people, both in America and elsewhere, who are obnoxious, selfish, mad or bad. Yet on closer examination, many of the rich, especially in America, are increasingly alert to the risk that wealth often turns people into selfish swine, and are searching for a meaning beyond money, though not incompatible with it—for themselves and, even more, for them to pass on to their children, so that those children will not be utterly spoilt by the wealth they inherit. There are still plenty of greedy big spenders out there, but a growing proportion of the rich now seem to feel that perhaps they should be working for a better society, however they choose to define it.

Why would this idea flourish in America, of all places? A tax system that encourages charitable giving may help. So, too, may a cultural tradition that abhors idleness and does not look to government first to provide the infrastructure of community life—and that honours those who give generously, instead of merely accusing them of trying to buy favourable publicity.

“Rather than trying to constrain the rich, as they have done for the past century, populists ought to look at the freedoms the rich enjoy and try to make them more generally available. In this, they might find powerful allies amongst the rich themselves,” argues Keith Hart, a British economic anthropologist and author of “Money in an Unequal World”. In future, successful campaigns for social change may require both a mass movement and some very wealthy backers—much like the free-trade and anti-slavery

movements of the 19th century, he suggests. “To succeed in changing society, best make friends with some capitalists,” he says. One cause he thinks could prove particularly attractive to the meritocratic rich might be an attack on global inequality of opportunity.

A unique advantage of being very rich is the power to bring about single-handedly the sort of change that would otherwise require a broad social movement. Bill Gates’s campaign to get the poor vaccinated is one example. That should make the rich attractive allies for anybody trying to shape society—and indeed they are increasingly being sought out, albeit often in secret. The main consequence of the bash-the-rich rhetoric of much public discourse, particularly outside America, may be to discourage them from putting their wealth to use for the common good, or to drive their giving underground. How much better to welcome the wealthy into public life with open arms, and to debate constructively with them how best to put their resources to work, on condition only that they conduct their activities transparently. That, in turn, is most easily done under a fiscal regime that requires them to pay a fair but not excessive amount of tax.

In 1930, John Maynard Keynes predicted that, some day, each person, as he achieved material comfort, would be confronted for the first time with his “real, his permanent problem—how to use his freedom from pressing economic cares, how to occupy the leisure which science and compound interest will have won for him, to live wisely and agreeably and well.” For a growing number of rich people, that day may have arrived. With luck, many of them will adopt solutions that will also benefit society at large.

"Economic Possibilities For Our Grandchildren”, by John Maynard Keynes. 1930.

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Acknowledgements and further reading

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As well as those mentioned in this survey, the author would like to thank in particular Jim Poterba of MIT; Andrew Dilnot of the Institute for Fiscal Studies; Robert Monks; Tamara Totah of DietSmart.com; Roy Bingham of Health Business Partners; Marlene Hess of J.P. Morgan; Raymond Baer of Bank Julius Baer; Peter Hero of the Community Foundation Silicon Valley; Jay Ritter of the University of Florida; Scott Weiss; and the Milken Institute.

Books cited in this survey, plus a few others that are worth dipping into (with links to buy from Amazon.com):

"The Virtue of Prosperity. Finding Values in an Age of Techno-Affluence". By Dinesh D'Souza, Free Press, 2000. A readable and thorough analysis of the rise of the new rich, and the opportunities and problems created by techno-affluence. An excellent introduction for anybody interested in this subject, though it suffers slightly from its tone, which is decidedly pre-dotcom-bubble-bursting. Having established that the new rich do not have the answer to their search for happiness, it drifts off rather unsatisfactorily into an attack on designer babies. See also "Bobos in Paradise. The New Upper Class and How They Got There", by David Brooks, Simon & Schuster, 2000. A fascinating and witty description of America's wealthy at the turn of the century, contrasting them with earlier generations of rich people, and noting how they are a paradoxical fusion of the bohemian and bourgeois (hence “Bobo”).

"The Mystery of Capital. Why Capitalism Triumphs in the West and Fails Everywhere Else", by Hernando de Soto. Basic Books in the US; Bantam/Randon House in Britain. The most intelligent book yet written about the current challenge of establishing capitalism in the developing world. Mr de Soto draws lessons from America's capitalist development to show what needs to be done. Above all, developing nations must recognise and protect the property that many poor people have created, but which is currently of uncertain legal validity, and thus is of little use in securing the loans necessary to invest in personal or business development.

"The Winner Take All Society: Why Those at the Top Get So Much More Than the Rest of Us", by Robert Frank and Philip Cook, Penguin, 1996. An excellent, if unenthusiastic, description of the economic forces that are enabling a small number of highly successful people to earn vast salaries whilst other scarcely less talented people in the same business barely scrape by. See also "Luxury Fever", by Robert Frank, Princeton University Press, 2000. An exploration of the orgy of consumption in which the rich indulge themselves.

"The Wealth Creators. The Rise of Today's Rich and Super-Rich. How the Really Big Money Was Made", by Roy Smith, St Martin's Press, 2001. An easy-to-read analysis of how America's richest people made their money, and why their success may now be replicated in the rest of the world. See also "How to be a Billionaire. Proven Strategies from the Titans of Wealth", by Martin Fridson, John Wiley, 2001. This exposes, without the usually empty flattery, the strategies that made some of today's billionaires so wealthy. The list of skills includes a willingess to break established and often popular social conventions and to beat up on the unions. For a broader historical sweep, try "The Rich and How They Got That Way", by Cynthia Crossen, Crown Business, 2000. This entertaining and fascinating book uses individual case studies to tell the story of the wealthy from Machmud of Ghazni in the tenth century to Bill Gates.

"Does Atlas Shrug? The Economic Consequences of Taxing the Rich", edited by Joel Slemrod, Harvard University Press, 2000. The proceedings of a conference in which leading economists examined the impact of changes in taxation on the rich. The title refers to Ayn Rand's notion that it is the rich and successful who carry the rest of the world on their shoulders, and that heavy taxation might cause them to stop trying so hard, or perhaps go on strike. An accessible read for an academic publication, with lots of fascinating data.

"The Rich Die Richer and You Can Too", by William Zabel, John Wiley, 1996. A hugely entertaining guide to tax and estate planning, full of juicy real-world tales of people who got it wrong, and some surprising ones (Jackie Kennedy, for instance) who got it right. Still a must-read, despite being five years old - though Mr Zabel would do the rich a big favour by updating it to include the likes of Anna Nicole Smith.

"Myths of Rich & Poor. Why We're Better Off Than We Think", by Michael Cox and Richard Alm, Basic Books, 1999. A fiercely argued counter-blast to those economists who doubt that as the rich of America have got richer, the poor have too. Makes the intriguing argument that growing inequality encourages innovation, because most new products are initially very expensive. The rich are the only people who can afford them, and so cross-subsidise the development costs for the poorer majority, who get to buy the goods later at much lower prices.

"Money in an Unequal World", by Keith Hart and His Memory Bank, Texere, 2001. A fascinating, if meandering, tour de force on the role of money, from the dawn of time and into the future. A book to be dipped into often, rather than read cover to cover. Half the ideas in it are brilliant, some may prove wildly wrong - and it may not become clear for years which are which.

"Generation to Generation. Life Cycles of the Family Business", by Kelin Gersick, John Davis, Marion McCollom Hampton and Ivan Lansberg, Harvard Business School Press, 1997. Probably the best study available of family firms, and how they rise and fall.

"The Wealth of Nations", by Adam Smith, 1776 (free text version from bibliomania). The classic defence of market forces, the invisible hand, and of why inequality in a properly functioning market system is probably not something to worry about. "The Theory of the Leisure Class", by Thorstein Veblen, 1899. Another classic, but a wrong-headed one, arguing that as people get richer they become more idle and useless. In practice, the rich seem increasingly aware of the perils of leisure, and work at least as hard as anybody else. In America, work is the new leisure!

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E-strategy brief: Cemex

The Cemex Way

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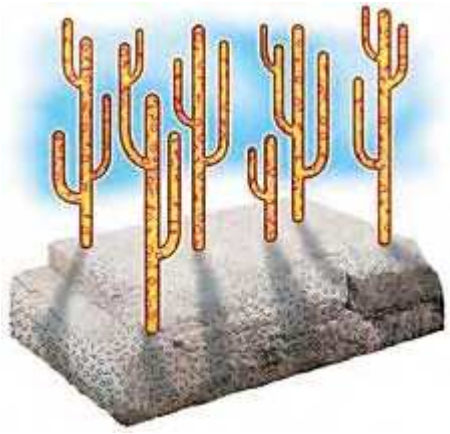
In our fifth e-strategy brief, we look at a rarity: a company in the industrialising world that has used e-business to steal a march on its rich-world rivals



OF ALL the countries and all the industries you could choose, Mexico and cement might seem to be the most unlikely combination to produce an agile, efficient, e-business pioneer. Yet Cemex is just such a company. It is rapidly spreading across the globe, and it is more profitable than either of its two big international rivals—France's Lafarge and Switzerland's Holcim (known until recently as Holderbank).

The Mexican company owes its success partly to the fact that, unlike its European rivals, it concentrates on developing countries. Profits there are greater because in such markets most cement is sold in bags for small-scale building, rather than in big ready-mixed quantities.

But the company also owes its success to what is known as "the Cemex Way". This corporate philosophy involves wholeheartedly embracing new technology and imposing tightly controlled standards worldwide, for both its technology and in-house management techniques.

Cemex's ability to apply this philosophy rests on a fortuitous mix of modest beginnings, good timing and the technology fetish of the company's chief executive, Lorenzo Zambrano, now reckoned to be Mexico's second-richest man. "I could say that I had a vision," says the jolly, 56-year-old Mr Zambrano, "but it doesn't really work that way."

A grandson of the man who founded Cemex in 1906, Mr Zambrano spent 18 years rising through the ranks before he became the boss in 1985. On his way up, he discovered the value of information. He wanted to make the plants that he supervised more efficient, but he chafed at the lack of ready data on how well they were performing. So he set up a small team of programmers to come up with ways to generate automated plant reports.

Not long after taking the helm he created something that Cemex had never had before—an information-technology (IT) department. The company began automating plant operations, and then its sales and accounting as well. At the end of the 1980s, it set up a satellite network so that it could transmit all the internal data to its headquarters in Monterrey, Mexico's dusty northern business capital.

Naturally, automation reduced staff costs: a handful of people can now run a big cement plant. Even such things as quality control can be handled automatically by machines that extract samples from the production line, slice them thin, analyse them by laser and spit out the results on a screen.

More valuable than the reduced headcount, though, was the data which the automation produced. Mr Zambrano could check sales figures or kiln temperatures on the network, and then use his latest toy, e-mail, to ask managers why their units were not keeping up to scratch. The company's first pilot e-mail system was launched in 1991. In 1992, it switched to Lotus Notes, which it still uses today.

There was resistance to the changes, especially to the e-mail; but open information and easy communication together brought about a shift in the corporate culture. Knowing that they were being watched, employees began to strive for improvements. At the same time, Mr Zambrano sought to make his managers receptive to new ideas from below. "IT frees up everyone's imagination," he says.

This upset Mexico's hierarchical, do-not-question-the-boss traditions. But it was a good moment for such an upset. Mr Zambrano took the helm just as Mexico's protectionist economy began to open up, leaving many family firms, stuck in their old ways, struggling to compete. He took the opportunity to grow by buying other, less agile Mexican firms.

At one stage he fired the company's top management—although it was hard, he remembers, to attract new talent. He won people over by promising them the chance to move around a lot within the firm, although at the same time he reduced the choices available to them by getting rid of the group's sidelines in hotels, petrochemicals and mining.

Gradually, computerisation spread throughout the group. Cemex has never had a big mainframe, relying instead on distributed, interconnected systems that share information across the company. These allow top managers to see what is going on, but they also give lower-level employees some access—enough to allow "a healthy degree of competition" between different units, says Hector Medina, Mr Zambrano's number two.

With the arrival of the Internet, the transparency spread outside the company, provoking some complaints from within that it was making too much information public. Cemex is, indeed, "one of the most investor-friendly companies in Latin America," says Gordon Lee, a New York-based analyst with Goldman Sachs, an investment bank.

Cemex is now pushing the information culture even further, putting computers with Internet access into its employees' homes. Cynics might see that as a sinister attempt to keep them chained to their work. Cemex sees it as a philanthropic gift to the employees' families and an investment in the future by spreading IT further.

Mix and match

Connectedness has also transformed many of the company's internal processes—most notably the delivery of ready-mixed concrete. Getting mixer trucks from the plants to the building sites at the right time, with cement needing to be poured within 90 minutes of mixing, is always logistical hell. But by putting a computer and a global-positioning-system receiver in every truck, and then combining their positions with the output at the plants and the orders from customers, Cemex has been able to produce a system that not only calculates which truck should go where, but also enables dispatchers to redirect the trucks en route.

That has reduced the "window of time" for delivery from three hours to under 20 minutes, even with the chaotic traffic and the last-minute cancellation of orders that are typical of Mexico city. It has enabled each truck to meet many more orders per day.

The real power of its IT, however, only became clear when Cemex grew big enough to expand abroad. Some 55% of its holdings are now outside Mexico. Its first purchase was two Spanish cement makers in 1992, and it has since moved into Asia, South and Central America and Egypt.

Last year it took a big bite north of the border by buying Southdown, America's second-biggest cement manufacturer, for $2.8 billion, and in May of this year it bought a Thai company, Saraburi Cement. At $73m, that was a much smaller purchase, albeit one that was more in keeping with the group's emerging-market strategy.

In each case, "post-merger integration teams"—ie, executives armed with laptops—were dispatched to analyse the new acquisition, to cut costs, and to harmonise its technical systems and management methods with Cemex's. The Cemex Way specifies everything, down to the make of computers that employees must use. It can seem authoritarian at times, but it does at least ensure that communication across the company is seamless.

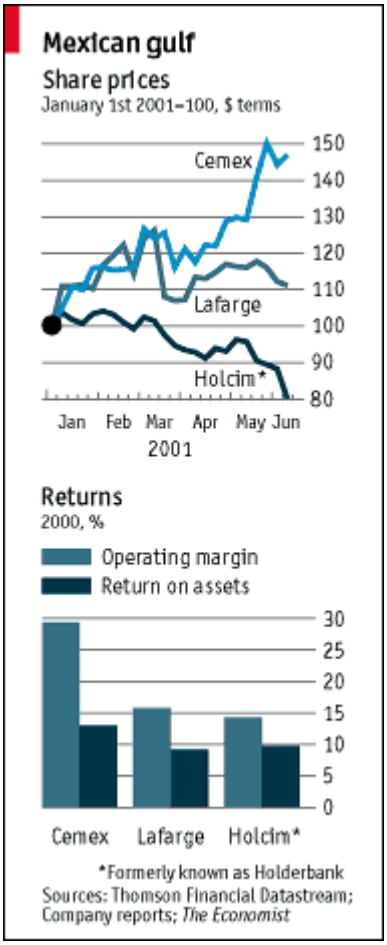
And it yields some welcome savings. According to Mr Zambrano, improving logistics at Southdown, already a fairly well-run firm, will save $15m a year, in a company that makes pre-tax profits of $280m. Moreover, with practice, the pace of integration has speeded up. Turning Valenciana and Sanson, the Spanish companies, into true subsidiaries took 18 months; Southdown, much bigger, was substantially "Cemexed" within four.

The fact that Cemex developed its “way” before it started expanding abroad has also given it an edge over Holcim and Lafarge, both of which had foreign subsidiaries long before the communications revolution began. It has been much harder for them to overcome institutional inertia and to unify their widespread information systems.

Cemex’s growing presence in developing countries gives it two other advantages, besides fatter margins. First, hundreds of thousands of bags labelled “Cemex” are a good way to make the company’s brand better-known. And second, it has had to deal with lots of small distributors rather than a few large ones, which has given it a powerful incentive to computerise its logistics and, eventually, to shift most of its transactions online.

This is the direction in which things are now moving. Last year, the company spun off its internal IT arm, Cemtec, and joined it with four other Spanish and Latin American firms to create Neoris, an IT consultancy. Neoris is now part of CxNetworks, a Miami-based subsidiary that Cemex wants to use in order to turn itself into an e-business in every way possible. Also part of CxNetworks are Construmix, a construction-industry online marketplace, and Latinexus, an e-procurement site.

How much this fits into Cemex’s overall development, and how much it was just an opportunistic attempt to benefit from the tech-stock boom, is uncertain. Some analysts think that Cemex was simply hoping to boost its stockmarket valuation, which it has long considered too low, given that it is more profitable than its more highly valued competitors. Not surprisingly, Cemex denies this. But in any case, since the dotcom market collapsed the question has become moot—and Cemex’s market valuation has continued to go up regardless (see chart).



Although Cemex is undoubtedly at the cutting edge of IT, it still has some way to go in what it calls “e-enabling”, something which Neoris will be in charge of. The goal is for all the company’s operations to become web-based, with all its employees having access to their own files, the company’s data and outside information through a single, personalised portal. Operations will be centralised through the Internet, even though the management teams themselves may be spread across the globe.

Corporate finance is already run in this way, and procurement, sales, distribution, and supplier and customer relations are also intended to become as Internet-based as possible. By the end of this year, Cemex plans to be halfway there. Ultimately, Mr Zambrano hopes that putting the company online will save it some $120m.

On the sidelines

All that should keep Cemex a jump ahead of its competitors, at least for the time being. Its aim is not necessarily to get bigger than them, only to stay more profitable. And although they are adopting new technology too, Cemex’s rivals will have trouble catching up.

But what can Cemex make from its e-business sidelines? Juan Pablo San Agustin, the brash young boss of CxNetworks, sees the greatest promise in helping other companies to “e-enable” themselves, the job which Neoris does. Mr Lee at Goldman Sachs agrees: “The part where there’s existing cashflow that should see growth is Neoris.” Latinexus, he says, may have a future too, since business procurement in Latin America is generally inefficient and sometimes murky, with lots of middlemen.

As for Construmix, the construction-industry portal, Mr San Agustin thinks that its future lies not simply in buying and selling online, but in providing other services for customers who already buy Cemex cement. For instance, it could create an online meeting-place for everybody involved in a particular construction project. The blueprints could be put on the Internet and be updated online. The contractors

and suppliers would then be able to consult an up-to-date version at all times. Construmix might also become a place to sell insurance, financing and other ancillary services.

Whether all this takes off remains to be seen. Having hoped to take CxNetworks public before the market crashed, Cemex now has to finance the venture's development alone. Since its Spanish purchases, the company has had a reputation for getting heavily into debt. That has been one reason for its low market price in the past.

Another factor has no doubt been a traditional wariness about investing in an emerging-market company—although Cemex executives lose no time in claiming that its debt rating is better than that of the Mexican government. For now, though, CxNetworks needs relatively little new investment.

Despite the economic slowdown in North America, where Cemex makes three-quarters of its profits, analysts remain bullish; in the first quarter of this year, the group's net sales were up by 19% on the previous year, and by 34% in North America.

At home, meanwhile, the group's future also looks pretty secure. In one of his more populist moments, Mexico's new president, Vicente Fox, promised that every peasant shack in the country would have its mud floor cemented by the time he leaves office.

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Recording industry

Big Music fights back

Jun 14th 2001 | NEW YORK
From The Economist print edition

The Internet was supposed to loosen the big record companies' grip on the music market. It did, but only for a while

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Reuters

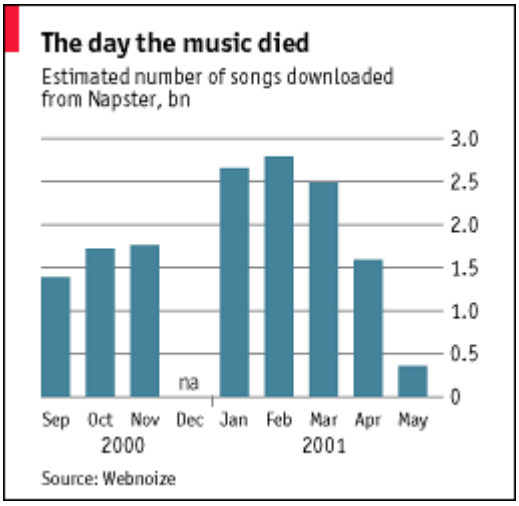
"RECORD companies stand between artists and their fans. We signed terrible deals with them because they controlled our access to the public. But in a world of total connectivity, record companies lose that control...Artists can sell CDs directly to fans. We can make direct deals with thousands of other websites and promote our music to millions of people that old record companies never touch."

So declared Courtney Love, an American rock musician, in a speech in New York a year ago. Those were heady times, when the web guerrillas plotted the downfall of the tyrannical record companies. Music-lovers were already sharing favourite tracks online with impunity, sending the big labels into a spin. Thanks to the Internet, a bunch of pimply teenagers with a computer would be able to post their music online, and turn themselves into rock stars. With no need for marketing, and nothing to make or distribute, what would be left for the record companies?

A year on, matters look rather different. Most of the defiant little upstarts that so shook the labels have either collapsed or been bought or shut down. Late last year, Bertelsmann, a German media giant, acquired the right to buy a majority stake in Napster, the pioneer of file-sharing and an American icon of online defiance, at the very time that Bertelsmann's own music division, BMG, along with the other four big record groups—EMI, Sony Music, Warner Music and Vivendi's Universal Music—was suing Napster for copyright infringement. Even executives at New York-based BMG were stunned by the deal.

Napster, meanwhile, is under a court order to eliminate all copyrighted files. It promises to convert itself into a subscription business by July. The more Napster snuffs out illegal files, the less people are using it: the number of songs downloaded from it fell from a peak of 2.8 billion in February to 360m in May (see chart).

The most stunning recent example of the record companies' volte face came in May, when Vivendi Universal paid $372m for MP3.com. Only last year, Vivendi was fighting the San Diego start-up for copyright infringement. Now, Michael Robertson, MP3.com's boss, who had promised to upset the record majors by breaking unsigned artists on the web, joins the Vivendi crew in their swanky offices on Park Avenue as "special adviser" to Jean-Marie Messier, Vivendi's boss. In short, the five big music companies, which jointly control over three-quarters of the world record market, are regaining their grip.



The critical test of whether they can keep it will come this summer, with the launch of two new subscription services. Sony and Vivendi, whose roster includes Eminem (pictured above), Limp Bizkit, Shaggy and U2, are jointly setting up pressplay, formerly known as Duet. This will offer secure, on-demand downloading of music via, for example, Yahoo!, a web portal. AOL Time Warner, which owns Warner Music, EMI and Bertelsmann, along with RealNetworks, will launch their own service, called MusicNet. This will act as a wholesaler of downloadable music, supplied by the three labels, to online retailers, including RealNetworks itself and AOL's new music-subscription service.

MusicNet will also license music to Napster—but only if Napster can prove itself a reliable policeman of copyright, and secure.

All of this looks like the setting for business as usual. Indeed, growing alarm at the tightening grip of the big five prompted the European Commission this week to announce a competition inquiry into MusicNet and pressplay.

The long and winding road

So was all the effort by Napster, MP3.com and other one-time rebels wasted? Far from it. Without Napster, the online jukebox would still be a distant dream. Although teams of boffins at the big music companies had been pondering the future of digital music distribution for years, the record majors were slow to react, treating the technology as a threat not an opportunity. As one executive puts it: “The big record companies are like big ships: they don’t move fast. They were happy making CDs. They just didn’t get it.”

Even now, there is no legal subscription service that allows music-lovers instant, unlimited access in the way that Napster did. Though both pressplay and MusicNet want to license the music from the other’s joint-venture partners, each now offers only its own. Moreover, each will contain security devices that limit the use or copying of any downloaded track. One reason for this reluctance is that nobody has yet worked out how to make money out of digital music distribution. And it is far from clear that the economics will stack up.

The new subscription services will attract a critical mass of paying customers only if the charges, at least initially, are low. A recent survey by Webnoize, a research firm, suggests that students, who listen to music on their computers nearly as much as they do on a stereo, would be ready to pay only about $10 a month. Even at $20-30 a month, for unlimited downloads, the record companies could expect a steep drop in revenues per track: consumers in America now pay over $1 per track on a CD album, which will often contain songs they would never choose to pay for. Pricing is also complicated by ongoing, unresolved talks with musicians and songwriters over royalties.

Yet record companies can scarcely afford this revenue squeeze. For one thing, CD sales, worth $37 billion worldwide, have been flat for the past five years, and margins are under pressure. For another, the music industry is a peculiar and unpredictable mix of fashion, branding and betting—with a pretty lousy hit rate. The average record label loses money on a staggering 90-95% of artists it signs, relying on a handful of mega-hits for its profits. Vast amounts of money are invested in promotion and marketing, most of which disappear down a black hole. This helps explain why, despite the appeal by Ms Love, it has proved so difficult to launch bands directly on the web.

In time, there may be cost savings from digital downloading, because manufacturing and traditional distribution costs will shrink. But the disc-pressing factories are not shutting yet: CD sales are still expected to make up four-fifths of music sales in 2010. So the immediate scope for big cost savings is limited, short of further consolidation among the big five. And the European Commission has twice indicated that it will firmly resist this.

The digital age may still leave the record companies with a job as talent-spotters and image-builders, and, for now, as manufacturers, but a question-mark remains over distribution. If the record companies can patrol the illegal market, and get enough reasonably priced music on to their new subscription services to lure those in a sulk about Napster’s demise, this problem becomes one for traditional CD retailers rather than the labels.

That is, however, a big if. For now, even as the record companies clamp down on the upstarts in the courts, former Napster users are drifting to other file-swapping services: Aimster, Audiogalaxy, KaZaa or Gnutella and its offspring, such as BearShare and LimeWire. The number of users logged on daily to Gnutella has quadrupled since March. The fastest-growing Napster clone is Audiogalaxy, which is picking up over 1m users a week.

These numbers are far from those achieved by Napster at its peak, but they are not trifling. Until now, music fans have had no real alternative. Once they do, most people, bar perhaps students, may prefer the legal option. But however much they pay, it will never match the anarchic thrill of the old Napster experience.

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Computing

Cluster adjuster

Jun 14th 2001 | SAN FRANCISCO
From The Economist print edition

A new way to bolt computers together

LISTEN to any software salesman and it is tempting to conclude that the world of information technology (IT) is a digital paradise. Yet just as in the real world, IT has its trade-offs—especially between "scalability" and reliability. Firms can combine several computers in order to sift through huge amounts of data. But adding new machines to such a cluster is complicated and makes the system more prone to crash.

The latest attempt to solve this dilemma was unveiled on June 14th by Oracle, the world's second-biggest software firm, as part of its new database, named 9i. If it works as advertised, the technology, called Real Application Clusters, will offer scalability and reliability in one package.

Because clusters are complicated, firms have used them mainly for specialised applications, such as data warehousing, in which groups of machines look for patterns in their stock of customer information. But the approach has rarely been used in areas in which information changes quickly, such as systems that keep track of orders or the supply chain, because it is hard to co-ordinate clustered computers working on fast-changing data.

Oracle's new technology makes clustering possible for this kind of corporate computing, by letting machines share the same short-term memory, or "cache" in technospeak, which makes it easier for them to stay in synch. Firms can quickly add new computers without having to rejig their systems or compromise on reliability. Even better, the more computers they add, the more reliable the system becomes. If one machine crashes, the cluster may work more slowly but it will not break down.

As fiddly as this sounds, it could fundamentally alter the economics of IT, says Carl Olofson, an analyst with IDC, a research firm. Start-ups, for instance, would no longer need to buy an expensive, oversized machine in order to ensure that they have enough computing capacity as they grow. Instead, they could start small and add cheap computers as necessary. And bigger firms would no longer have to install bulky, expensive computers powered by the Unix operating system in order to be sure that their applications were always available and could withstand the onslaught of millions of users.

This could spell bad news for the firms that sell Unix systems, mainly Sun Microsystems, Hewlett-Packard and IBM. Why spend a lot of money on these computing workhorses if a collection of cheaper machines can do the job just as well? At a time when companies are thinking hard about the most efficient way to spend shrinking technology budgets, programs that allow them to strap small, cheap computers together could be just what they need.

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Workers' rights in the EU

Inform, consult, impose

Jun 14th 2001 | BRUSSELS
From The Economist print edition

A new directive has unions cheering and company bosses fuming

IN A recent speech on the future of the European Union, Lionel Jospin, the French prime minister, argued that, after a decade in which the EU's emphasis had been on building a single market, it was time to concentrate on "social Europe". So this week the French were delighted by an agreement of the Council of Ministers on a new directive, strengthening the obligations on European firms to "inform and consult" workers' representatives about company strategy.

Less delighted was UNICE, the European employers' federation, which regards the directive as an unnecessary new burden on business. As for the Confederation of British Industry, it was positively outraged, pronouncing itself "deeply disappointed" by this new infringement on managers' right to manage. Meanwhile, many economists fear that the directive may make Europe's stiff labour markets even less flexible, just as growth in the continent's main economies slows.

Even without the new directive European law already obliges multinational companies to consult workers about certain corporate actions—for example, mass layoffs. But the new directive will greatly expand the number of companies affected, and the extent of their obligations. By 2008, all companies with 50 or more employees in the EU will be obliged to "inform and consult". The obligation will now also extend even to companies that do not operate outside their home country. And the consultation involved will have to be "ongoing", rather than simply occurring when big business decisions are in the works.

The directive has not yet passed its final hurdle. It still has to be approved, and it may be amended, by the European Parliament. But the parliament, backed by the European Commission, is likely only to try to strengthen it. Anna Diamantopoulou, the commissioner in charge of social and employment affairs, wants the directive to include tougher legal sanctions against employers that breach its provisions, and the parliament is likely to oblige. European governments will then have to bargain over some sort of compromise text.

There is still some vagueness about precisely what information and consultation entail. In Britain and Ireland, some companies have expressed fears that the new directive will, in effect, mean compulsory unionisation or the formal recognition of works councils—bodies that are embedded in German corporate life, but unusual in Britain.

A European Commission spokesman insists, however, that "there is no policy drive to reactivate unionism". The directive makes references to countries implementing the legislation in line with their own national traditions. Some even speculate that setting up an intranet chat-room for the review of company policy may be enough to satisfy European law. But the reality is likely to be that only time—and legal precedent—will establish how far the new rights will go.

The passage of the worker-consultation directive is a bitter pill for the British, who have fought it for several years. When Tony Blair came to power in 1997, he ended Britain's opt-out from European social legislation, arguing that it was better to win the arguments than to stand on the sidelines. This argument, however, is one that Britain has comprehensively lost—and this despite the call at last year's Lisbon summit for more flexible European labour markets. By June 11th, the Blair government found itself in a minority of one against the other 14 EU members. Because Britain no longer has an opt-out, it was powerless to prevent the directive being imposed on it by majority vote. Rather than face the humiliation of a defeat in the council, Britain negotiated a face-saving concession—essentially delaying the evil day of full implementation—and declared itself satisfied. Whether British bosses will be so cheery is another matter.

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Face value

The wrong trousers

Jun 14th 2001
From The Economist print edition

Linda Wachner has been toppled by hubris and poor governance as much as by changes in the fashion industry

FOR a woman who is used to wearing the trousers as well as making and selling them, these must be hard times. On June 11th Linda Wachner had to watch Warnaco, the clothing group that she has run for the past 15 years, file for bankruptcy protection with debts of $3.1 billion, some 30% more than the value of its assets. The company, famous for making Calvin Klein jeans, Speedo swimwear and lingerie, is now in the hands of a "chief restructuring officer" and a banking consortium that has provided $600m of new money.

The first female boss of a Fortune 500 company, Ms Wachner was lionised in 1992 by *Fortune* magazine as America's most successful businesswoman. She soon became not just one of fashion's most powerful executives but also a leading Manhattan socialite. Soon, however, she may be looking for a job. With Warnaco's shares down from $44 in 1998 to 39 cents, her 22% stake in the company could turn out to be worthless. On June 12th, with Warnaco facing delisting, she resigned as a director of the New York Stock Exchange—bizarrely, only a week after she had been re-elected.

This bitter end belies Ms Wachner's early promise. A native New Yorker who attributes her toughness to an attack of scoliosis that put her in a bodycast for a year when she was 11, Ms Wachner started as a bra buyer at Macy's and later helped to rescue Max Factor, a cosmetics group. In 1986, three years after the death of her much-older clothing-executive husband, she led a hostile buy-out of Warnaco, a struggling clothing firm. Adding licensed ranges from Calvin Klein and Ralph Lauren, she brought designer clothes to the masses. In 1991 she took Warnaco public. Six years later she bought the company that makes Calvin Klein jeans, putting her in charge of a third of the designer's goods. At the time Mr Klein was happy enough, as annual sales of his stable's underwear shot up sevenfold to $340m.

Warnaco's revenues, boosted by its acquisitions, grew from $590m in 1986 to $2.25 billion last year. Over the past couple of years, however, the company has lost market share. In a flat market, Warnaco's sales of underwear dived by 18% in the first quarter of this year; those of Sara Lee, a big rival, grew by 6%.

This loss of business is largely down to serious strategic errors. Ms Wachner initially underestimated the importance of big discount stores such as Wal-Mart, only to woo them frantically when it was too late, dumping inventory on them at knock-down prices to hit financial targets. This alienated traditional department-store customers and angered Warnaco's licensors. Mr Klein, whose clothing accounts for about 40% of Warnaco's sales, sued both the company and Ms Wachner, alleging that selling through discounters had cheapened the brand. The two managed to make up in January with a public kiss minutes before the trial was set to open, but the lawsuit was a public-relations disaster for Warnaco.

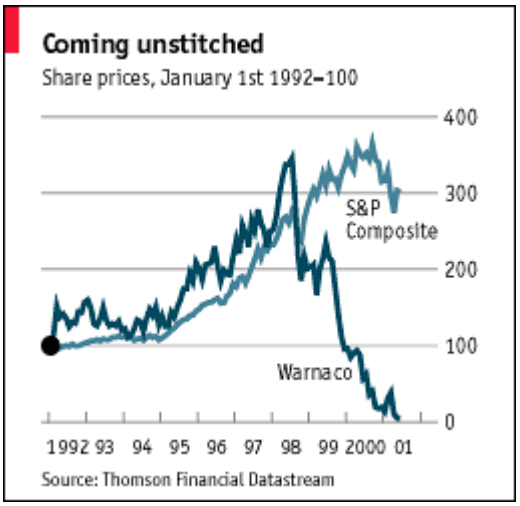
Empress Linda

Ms Wachner has compounded these mistakes with a personal style that is most kindly described as imperious. During their battle, Mr Klein called her "a cancer" and her language "disgusting". Industry executives recount tales of her dressing down staff. One says unkindly that the only employees who last at Warnaco are those "who were abused as children". Staff turnover has certainly been high. Over the past five years, Ms Wachner has had three chief financial officers at Authentic Fitness, one of her purchases; there have been five presidents of Calvin Klein Kids in three years. The problem, says one

leading American pension-fund manager, is that she has a poor understanding of the business. Kurt Barnard, a retail consultant, goes further: “She led this firm into the mud. Her conduct and miscalculations have been deplorable.”

Nor has there been much financial prudence. Warnaco’s liquidity problems are partly the result of an over-ambitious acquisition spree. Attempts at “channel-stuffing” (pushing more merchandise on to customers and distributors than they can sell) have also backfired. This combination pushed the group into a net loss of $338m for 2000, against a $98m profit the previous year. It has also unleashed a series of lawsuits from disgruntled shareholders.

Greed has played a part too. Ms Wachner has always ensured that she was paid well. In 1994, admittedly when Warnaco was doing rather better, she collected $10m—more than Jack Welch, General Electric’s legendary boss. Even last year, with Warnaco already in trouble, Ms Wachner was paid $2.8m and continued to enjoy the trappings of success, such as helicopter commutes from her Long Island home. To top it all, she negotiated a massive “golden parachute” worth as much as $44m—four times the firm’s current cash—which has in effect made her unsackable.



Warnaco’s board, recently voted one of America’s worst (by *Fortune*, ironically), has been unwilling to restrain these excesses. One reason, according to an industry source, is that many of its members depend on Ms Wachner’s social connections for lucrative board positions elsewhere. Even the appointment this year of some heavyweights—notably Harvey Golub, former chairman of American Express, and Frank Olson, boss of Hertz—cannot disguise the board’s “complete failure of corporate governance”, fumes Ted White at CalPERS, America’s largest public pension fund.

As for Warnaco, its future looks grim. Whether Ms Wachner clings on or not, her empire is most likely to be broken up into its constituent brands, with shareholders, including her, losing their entire investment. It would, perhaps, be a fitting end to such a tale—but one that, unfortunately, will only hinder the cause of those female executives whose brightest role model she once was.

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China's postal monopoly

Dubious courier moves

Jun 14th 2001 | BEIJING
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If the competition is doing well, bully it

AS CHINA'S economy opens up, its coddled state-owned monopolies know that they must prepare for greater exposure to the rigours of the marketplace. But some are in denial. A prime example is the postal monopoly, China Post. Rather than adapting to competition, it is trying to close it down.

EPA

A warning to rivals

In recent months, officials from the State Post Bureau—the agency that controls China Post—have visited rival firms in several provinces and ordered them not to handle express mail. One of the targets was a joint venture between DHL International and Sinotrans. The business licence of Federal Express's Chinese agent in the southern city of Dongguan is being reviewed. And UPS has had two of its international shipments blocked. "This issue is affecting all the air-express companies operating in China," says David Cunningham, president of FedEx Asia Pacific.

China Post argues that it alone has the right to handle express-mail services, whether within China or internationally, and whether business or private. But the Ministry of Foreign Trade and Economic Co-operation, which approved the operations of foreign courier firms in China, takes a different view. It argues that the law allows the government to make exceptions to China Post's monopoly. This it did in 1995 when it first allowed foreign firms to handle international business-mail deliveries by forming joint ventures with Chinese freight forwarders. In fact, China has allowed such business since the 1980s.

As a result of foreign competition, China Post's share of the international express-delivery market has been whittled down to 40%. The company is likely to come under still greater pressure when foreign courier firms win the right to acquire majority ownership of their joint ventures in China and, within four or five years, to operate independently. Domestic courier companies have also mushroomed in recent years, many without official approval.

China Post appears unfazed by foreign operators' criticism, and postal officials have sternly defended the incumbent's stance. It involves, they say, a "serious question of principle" with wide-ranging implications for, among other things, China's politics and state security. But for all its political clout, China Post is unlikely to win this battle. The competition is too deeply entrenched and the market developing too fast.

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Mobile telephony

Nokia succumbs

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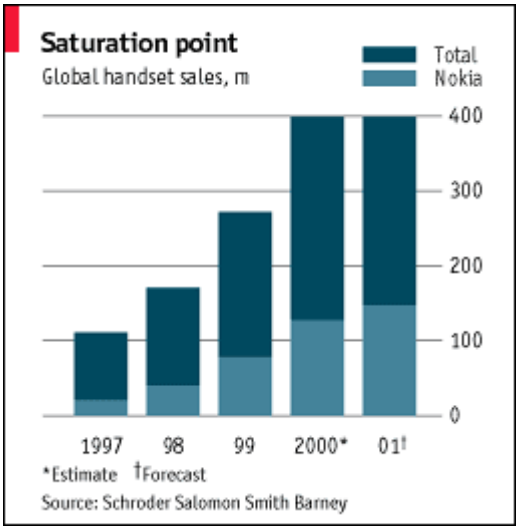
From The Economist print edition

The mobile-phone industry has reached another turning point

IT WAS proof, if proof were still needed, that no technology company is bulletproof. On June 12th Nokia, the world's leading manufacturer of mobile telephones, gave warning that its second-quarter profits would be lower than expected, and that annual sales growth, previously forecast at 20%, would in fact be less than 10%. Nokia's shares fell by 23%, though they later recovered slightly. Other telecoms firms' share prices suffered too, with the exception of BT, whose shares rose after news of a 3G network-sharing deal with Deutsche Telekom.

Nokia's announcement was portrayed by Jorma Ollila, the firm's boss, as an indication that the slowdown in the American economy is having knock-on effects in Europe. But this explanation is a red herring, says Mark Davies Jones, an analyst at Schroder Salomon Smith Barney. Although Nokia has been slightly affected by falling consumer demand in America, the real cause of its problems is that the market for handsets, which account for nearly three-quarters of its sales, is saturated.

The problem is that people are neither buying new phones, nor upgrading their old ones, as often as they used to. In part this is because network operators, most of which are struggling with huge debts, feel less inclined to subsidise handsets. But it is also because there is no compelling reason to upgrade your phone once it is small and sexy enough. The days of double-digit growth in handset sales are over: the number of handsets sold worldwide—400m last year, of which 32% were Nokia's—is not expected to rise this year (see chart). Any sales growth at Nokia this year will come from increasing its market share.



What now? The industry has a plan, which is to introduce new mobile-data services. Operators will benefit by being able to charge for these services (since revenues from voice traffic have stopped growing) and handset manufacturers will be able to sell everybody new phones. The problem is that the first incarnation of mobile data, Wireless Application Protocol (WAP) services, was a flop. So the industry's hopes are now pinned on a new technology, General Packet Radio System (GPRS), which is faster than WAP and offers "always on" connections.

On June 13th, the GSM Association, an industry standards-setting body, announced a scheme called the "M-Services Initiative", which defines a standard way to offer graphics and other multimedia content on GPRS phones. The idea is that these new features will encourage users to upgrade their handsets, and thus plug the gap before the arrival of 3G phones in a couple of years' time. The big operators and manufacturers, including Nokia, are backing the scheme, and the first handsets sporting graphics should be in the shops by Christmas. One way or another, this week could prove to be a turning point for the industry.

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Ford and Firestone

Nasser's nightmare

Jun 14th 2001 | DETROIT
From The Economist print edition

Ford's tyre problems continue to distract it from other big challenges

HENRY FORD and Harvey Firestone must be turning in their graves. On June 19th, the chief executives of the two companies they founded will appear at yet another congressional hearing into why Ford Explorer SUVs fitted with Firestone tyres roll over. More than 170 people have been killed in such accidents in America alone. John Lampe, the boss of Firestone, and Ford's chief executive, Jacques Nasser, are loth to sit side by side, perhaps lest they start hitting each other. But they have been brawling in public by other means since last month, when Ford announced the recall of 13m Firestone tyres, saying data showed they were suspect. This followed a compulsory recall last summer, when the tyres were first linked to roll-over accidents.

Firestone, owned by Bridgestone, a Japanese company, reacted to Ford's move by cutting ties with Ford and calling on the government to investigate safety problems with the Explorer itself. A study funded by Firestone has raised safety concerns about the vehicle's design. Ford, naturally, has rubbished the study. This week it said that Firestone tyres have shredded on 167 vehicles other than Explorers.

This could not have come at a worse time for Mr Nasser, who was once seen as Ford's wonder boy. Since last summer, the company has faced a sea of troubles. The Firestone affair tarnishes one of Ford's most important products—the Explorer accounts for roughly 10% of its profits worldwide. But sales of the vehicle have tumbled as competitors have launched well-received products. Overall, Ford's American sales for the first five months of this year were 11% below the same period last year, and its market share was down by about two percentage points.

Since taking the reins in January 1999, Mr Nasser has made plenty of promises about quality, safety and productivity, but recent studies question his record on all three. On June 14th a respected Detroit manufacturing consultancy, Harbour and Associates, revealed that the factories of the firm's arch-rival, GM, have become more efficient than Ford's, which used to enjoy a cost advantage of around $2,000 per vehicle. Given that GM is hardly the world's leanest manufacturer, Ford must feel it has been overtaken by a tortoise.

Vehicle quality is a worry, too. Last month, J.D. Power & Associates, a research group, released its latest quality survey—a crucial barometer of consumer perceptions; Ford had fallen to bottom position among the leading car makers. That was underscored by the five recalls (for faults unrelated to tyres) that its new Escape SUV faced during its first few months on the market. To avoid the same problem with the all-new Explorer, Ford tried delaying the vehicle's launch by nearly half a year. Yet it still faced two recalls within a month.

Mr Nasser has angrily denied rumours of an imminent shake-up of top management that might give the Ford family heir, William Ford, more say in the day-to-day running of the group. But even without a shake-up, the powerful Ford family will continue to make clear its concerns about the recent spate of problems—and Ford's shrunken share price. After all, it still owns about 40% of the voting shares.

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German railways

Private lines

Jun 14th 2001 | KIEL
From The Economist print edition

Bit by bit, private firms are taking business from Germany's state railway company

THE station in Kiel is no advertisement for rail travel: like most buildings that are being refurbished, it is an ordeal for both the eyes and the ears. The trains are more welcoming. Head south to Neumünster, or west to Husum and Bad St Peter-Ording, on the North Sea, and you will sit in new, spruce vehicles. As you gaze through their windows, you can listen to music piped to your seat (but bring your own headphones). If you do not have time to buy a ticket before your journey, never mind: get one from a machine on board.

These trains are owned by Nord-Ostsee-Bahn (NOB), which last November took over services on 177km (110 miles) of track from Deutsche Bahn, Germany's state-owned railway company. NOB, which has a ten-year franchise, is a product of a reform in 1994 that handed responsibility for local trains, plus an annual dollop of federal money, to the 16 *Länder* (states). Mainly, the *Länder* buy services through negotiated contracts lasting a few years, although there is a trend towards competitive tenders. DB Regio, part of Deutsche Bahn, still has over 90% of the market. However, some outsiders have fought their way in. Some are owned by the *Länder* themselves; one is part-owned by SNCF, France's state rail monopoly.

The biggest private operator, Connex, a subsidiary of Vivendi Universal, a French conglomerate, owns six regional passenger railways, including NOB. Connex also runs a big commuter network in south-east England, where passengers often complain about delays, cancellations and dirty trains. Dubious reputation? Not in Germany, where its subsidiaries are seen as plucky, efficient underdogs snapping at the big, bad Bahn.

Schleswig-Holstein, the state of which Kiel is the capital, is in the vanguard of change. It has already run tenders for 23% of its services (measured by train-kilometres). Deutsche Bahn's local market share has fallen from 90% to 75% since 1995. The next step, says Bernhard Wewers, head of LVS, the company that oversees local transport in the state, is for local politicians to decide whether to open bigger lines to tender. If they do, and if Deutsche Bahn does badly, its market share could fall below 50%.

The aim, says Mr Wewers, is to cut the state's costs, while improving services and so coaxing people out of their cars and into trains. When the state first asked Deutsche Bahn for cheaper services, he says, "they told us we were silly." Yet across Germany, he reckons, competition has cut costs by 10-20%. Rolling stock has to meet certain criteria: hence NOB's smart trains, and similar ones used by DB Regio between Kiel and Flensburg, on the Danish border. New stations have been opened. All this has helped push passenger numbers up by 18% since 1995.

Predictably, Deutsche Bahn and its new rivals do not always get on. One source of friction is the role of DB Netz, another division of the state giant, which manages the country's tracks. Bela Bergemann, NOB's marketing director, complains that, on one bridge where repairs are needed, trains can run at only 40kph, adding several minutes to the Kiel-Husum run. Hans Leister, head of Connex's passenger-train operations in Germany, accuses Deutsche Bahn of using its control of investment to sway the *Länder* towards DB Regio. Quite wrong, says Deutsche Bahn. Stefan Garber, a member of DB Netz's management board, says that the *Länder* would never allow Deutsche Bahn to tie infrastructure spending to train contracts.

Even-handed or not, DB Netz is also at the heart of a heated political argument. Kurt Bodewig, Germany's transport minister, thinks that Deutsche Bahn should not own both the track and the trains. Separate ownership, he believes, would foster competition (as in Britain's Railtrack, though not everybody would see that as a good model). Hartmut Mehdorn, Deutsche Bahn's pugnacious boss, is adamantly against the idea. The company's view is that separate ownership would make no difference to competition, and that, for technical reasons, it makes sense to keep the two together.

Deutsche Bahn's rivals do not necessarily want the company split up. If its market share could be drastically reduced, says Connex's Mr Leister, that would do just as well: the problem is the combination of track ownership and market dominance. He says that DB Netz's track-usage charges are now "fair". Until April, charges decreased with volume: fine for Deutsche Bahn, not so good for the rest. After intervention by the Federal Cartel Office, bulk discounts have been ended, in the hope of helping entrants. Not everyone is happy, however. Deutsche Bahn managers call the new system "reverse discrimination".

This leaves one crucial question: how can new entrants provide a better service than cash-strapped Deutsche Bahn and still make money? Lower overheads are a plus, says NOB's Mr Bergemann; and people are usually better motivated in a small private business than in a big state corporation. In a small operation, he says, problems can be dealt with speedily and by the people in charge. He makes the point, in a small way, when a train pulls into Neumünster: he strolls through the carriage, picking up discarded newspapers.

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Chinese aviation

One country, many routes

Jun 14th 2001 | HONG KONG
From The Economist print edition

Turbulence on flights between mainland China, Hong Kong and Taiwan

EPA

THE world's most travelled airline route connects Taipei and Hong Kong. This is a legacy of China's civil war, since Taiwan still prohibits direct flights to the mainland, forcing its businessmen to transit in Hong Kong on the way to and from their mainland factories. As China considers Taiwan to be a renegade province, moreover, landing rights are negotiated between the airlines themselves, with the governments in the background. Commercially and politically, this can get tense. So it was this week, when the latest landing-rights "arrangement" between Taiwan and Hong Kong expired (only countries can reach "agreements"). Instead of being renewed for another five years, it was simply extended by a few months, pending further discussions.

Awkwardly, this coincided with reports in Hong Kong's local press—which were unfounded, as it turned out—that the territory had struck a deal with Beijing to allow the two Hong Kong carriers involved in the Taiwanese negotiations, Cathay Pacific and Dragonair, to compete on routes to the mainland. In fact, Beijing and Hong Kong have agreed only to increase capacity on certain routes, but not to open them up to new carriers. That, however, may be only a matter of time, given the speed with which China's aviation market is changing.

Hong Kong plays a big part in these changes. Already a hub not only for Greater China but for much of Asia, it wants to strengthen its role. Several factors work in its favour. Location is one: unlike Singapore, for instance, Hong Kong is within reach of direct flights from America and close to the booming Chinese hinterland. Capacity is another: Hong Kong opened a giant new airport in 1998 and plans to list shares in it in the coming years. To attract ever more airlines, the government intends to liberalise landing rights—though only "gradually", it says. Last month, for instance, Hong Kong began to allow Air New Zealand to pick up passengers in Hong Kong and fly them to London.

It helps that Hong Kong's government, unlike most others in the world, has never owned or coddled its domestic airlines, and so confronts fewer interests stacked against liberalisation. Cathay Pacific, the territory's flag carrier, controls only about 30% of the landing slots at its home airport, far less than most incumbents elsewhere. So Cathay, one of Asia's best-run airlines, is already used to intense competition. Publicly at least, its managers favour liberalisation, as long as it is based on reciprocity, since a shrinking share of a growing market might still translate into more profit.

Friends or foes?

Ironically, however, Hong Kong's "motherland"—which officially includes Taiwan as well as mainland China—may prove to be Cathay's biggest challenge. Hong Kong now follows a policy of "one route, one airline" among its own carriers. This arrangement dates back to the 1980s, when Cathay bought Dragonair, the only other Hong Kong-based passenger carrier, and then divided routes between the two, so that they would complement rather than duplicate each other. Thus only Dragonair now has rights to the Chinese mainland, and only Cathay serves Taipei. In the 1990s, however, mainland Chinese interests took control of Dragonair, as Cathay sold down its stake. The two airlines now seem confused as to whether they are partners or rivals.

Increasingly, they are the second—and this could hurt Cathay. Wendy Wong, an analyst at Merrill Lynch in Hong Kong, estimates that Cathay gets about 12% of its revenues from its "golden route" to Taipei. On it, Cathay already faces competition from two Taiwanese carriers and from Thai Airways. If Dragonair

muscles in too, as analysts expect, Cathay will suffer. Its obvious escape is to win Hong Kong-mainland rights in return. It was this sort of horse-trading between Cathay, Dragonair and the authorities that was rumoured to be going on this week.

Without it, Cathay will have to think again. Buying a mainland carrier is one option. The trouble is that the turmoil that exists in Taiwan and Hong Kong is as nothing compared with the upheavals on the mainland. In April, Beijing announced plans to merge ten mainland carriers into three. Of these, Air China will become the national champion for international flights and will be listed in Hong Kong and New York. Its parent, moreover, also controls Dragonair—and the two may team up against Cathay. The two remaining mainland giants, China Eastern and China Southern, will dominate China's domestic routes. Cathay is already in talks with China Eastern, which is based in Shanghai. But some analysts fear that the Chinese may still regard Cathay, which is part of Hong Kong's Swire Group, as unacceptably "British".

There is an even bigger imponderable. Nobody knows when direct transport links between Taiwan and the mainland will become possible, but their desirability (and inevitability) have become totems of Chinese patriotism throughout Greater China. Officials in Hong Kong and managers at Cathay strive bravely to sound as enthusiastic about them as anyone else. Privately, however, they are worried that Hong Kong's days as a fast-growing hub may be numbered.

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The International Monetary Fund

Köhler's new crew

Jun 14th 2001 | WASHINGTON, DC
From The Economist print edition

EPA

Some hopeful signs for the future now that a new, high-powered team is to help the IMF's boss with his reforms

Get article background

HORST KÖHLER, head of the International Monetary Fund, is in an irrepressible mood. Barely a month after talk of a management crisis at the Fund—several top staffers, including his formidable deputy, Stanley Fischer, had said they were leaving—Mr Köhler has scotched the rumours by appointing a slate of top-flight replacements. And barely a year after taking over, Mr Köhler, who was nobody's first choice, is putting into place a broad, if not radical, overhaul of his institution. Emerging-market crises are not distracting attention from his reforms. And George Bush's Treasury team, whose initial rhetoric was about ending "bail-outs" for countries in trouble, has since taken a remarkably relaxed attitude, most notably over loans to Turkey. As a result, Mr Köhler may end up reshaping the world's most important international financial institution pretty much on his own.

The most senior appointment in the new team is Anne Krueger, a professor at Stanford University, former chief economist at the World Bank and a trade expert. She is to succeed Mr Fischer. Ken Rogoff from Harvard University, who is co-author of a canonical graduate textbook on international economics, is to head the research department. Tim Geithner, former under-secretary in the Clinton Treasury, is to run the Fund's heavyweight policy-review department. And Gerd Häusler, a former Bundesbank board member and chairman of Dresdner Bank's investment-banking arm, is to head a new capital-markets department.

By and large, these appointments have gone down well both inside and outside the Fund. The Fund's researchers are delighted about attracting an academic of Mr Rogoff's calibre. Mr Geithner is admired by those who know him as a practical, problem-solving bureaucrat. Though Ms Krueger was not Mr Köhler's original choice—rather, she was put up by the American Treasury—she is in many ways a Republican version of Mr Fischer. Like her predecessor, Ms Krueger combines an impressive academic career with previous experience in international institutions. Though she is partisan (she was, until this appointment, due to join Mr Bush's Council of Economic Advisers), Ms Krueger does not share many Republicans' ideological opposition to the IMF. In the wake of Asia's financial crisis in 1997-98, she publicly defended the IMF's role.

A few concerns remain. Staff know Ms Krueger to be a forceful character with strongly held views, and wonder how Mr Köhler, who has a temper of his own, will react. More seriously, some worry about who will become the Fund's chief firefighter in a crisis, a role that Mr Fischer all but monopolised. Ms Krueger's background is in trade more than in macroeconomics. Besides, some speculate, her age (she is 67) suggests a more limited appetite for jetting into every crisis.

With his experience in the Treasury Department under Larry Summers, Mr Geithner has the aptest background, but he is only 39 years old and, some Fund staff mutter, not even a real economist. While Mr Rogoff has the economic credentials, even IMF staff are worried that he is too academic ("a bit of a nerd") to thrive in the rough-and-tumble of policy fights.

Mr Köhler, on the other hand, betrays no such concerns. He is clearly delighted at his "excellent" team. He appears to be convinced that this new batch of outsiders will help him to continue his reform agenda. That agenda, laid out at the IMF's annual meeting in Prague last September, is about refocusing the institution on what Mr Köhler sees as its core mission: maintaining macroeconomic stability. In his mind, going back to basics requires a greater emphasis on capital markets and financial flows; a bigger effort to prevent crises, rather than simply to manage them; and a streamlining of the conditions the Fund attaches to its loans.

Institutionally, he has already made changes. The department headed by Mr Häusler, for instance, is to be responsible for the new capital-market focus. A new, informal consultative group, where top Fund officials talk regularly with top people in the markets, is designed to strengthen ties between the two. Long before Mr Köhler's arrival, boffins inside the IMF were working on sophisticated models designed to provide "early warning" of when a country was heading for a financial crisis. Although many of the technocrats are unwilling to put too much faith in such models, Mr Köhler now wants to integrate them into the Fund's efforts to head off crises. He wants to find ways to induce vulnerable countries to improve their policies, perhaps even by giving a public warning that a crisis is imminent.

Mr Köhler's biggest innovation may be in the area of "conditionality", that is, the strings that the IMF attaches to its loans. Since the mid-1950s, the Fund has demanded policy reforms in exchange for the money that it lends, but in recent years the number and nature of these conditions has greatly expanded. In particular, a welter of "structural" conditions has been imposed—reforms such as privatisation or trade liberalisation—that go far beyond straight macroeconomics. In the mid-1980s, the average IMF programme had two or three structural conditions. In recent years that has risen to 12 or more. Partly in response to widespread criticism that the IMF is too intrusive, and partly because he thinks reforms cannot work unless a country "owns" the policies itself, Mr Köhler is determined to streamline the number and nature of demands that the Fund makes.

The process is already well under way. This year's loans have had noticeably fewer conditions attached, and they have focused on reforms critical to macroeconomic success. But Mr Köhler wants to go further, towards a more co-operative, rather than dictatorial, relationship with his borrowers. Ultimately, he reckons, the Fund could even lay out a menu of policy options, and allow the borrowing country to choose from it.

Most of these reforms are going down well with the Fund's shareholders. Though some rich-country governments, and many Fund staff, worry about narrowing conditionality too much, "ownership" of reform is all the rage in development circles. And though many insiders fret about exaggerating the Fund's ability to head off crises, the focus goes down well with Paul O'Neill, America's treasury secretary, who has made a big deal about preventing, rather than merely responding to, crises.

Equally important for Mr Köhler, his biggest shareholder now appears to want to meddle less. The Summers Treasury was closely involved in the details of every big bail-out. Mr O'Neill plays a more distant role. A new team, and autonomy granted by shareholders, gives Mr Köhler an opportunity to push through his own agenda. But it means there is nobody else to blame if he blows it.

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Commonwealth Development Corporation

Two fingers to the poor

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Privatising Britain's development arm may not help those who need it

WHEN the British government set up the Colonial Development Corporation in 1948, the aim was to develop self-sustaining agriculture, industry and trade in the British empire. Renamed the Commonwealth Development Corporation (CDC) in the mid-1960s, its area of operation widened to the third world in general. Still, it kept its development mandate, especially for poor rural areas.

In 1997 Tony Blair, the Labour prime minister, declared the CDC a trendy "public-private partnership", the first of several attempts by his government to involve private capital in state-owned businesses. In the long run, the government still planned to keep a substantial minority stake, and the CDC was to carry on as a benign investor in poor countries. Its new mandate was to invest in sustainable and socially responsible projects that were also profitable. Its charter insists that at least 70% of its investments are in poor countries, with 50% in sub-Saharan Africa and south Asia.

At the time the idea of the changes was simply to raise capital from the private sector. A new management team, however, had different notions. Led by Alan Gillespie, formerly of Goldman Sachs, the new team found that CDC's assets, mainly loans, were in Africa, many of them farms and forests. They were long-term, labour-intensive agricultural projects run by local experts. Examples were a fish farm in Zambia, sugar plantations in Swaziland and tea estates in Kenya and Malawi. The trouble is that agriculture in Africa produces at best a return on capital of 8-9%, less than half of the 20% return demanded by the typical emerging-market investor. "With considerable reluctance", Mr Gillespie decided that agricultural projects must go.

The new company has been renamed CDC Capital Partners. Two-thirds of the staff, largely the agricultural experts in small African countries, were laid off. Offices were closed, and farms and forests prepared for sale. The new CDC went off in search of investment opportunities which, in the words of its chairman, Lord Cairns, "achieve higher financial returns demanded by private markets." It found them in telecoms, banks, health care, minerals, oil and gas, and property. New regional offices, manned by people who know more about making deals than growing pineapples, have opened in Egypt, China and Mexico. The company is looking for investors and aims for a partial privatisation in the next 18 months.

In the meantime, unease reigns. The CDC is wholly owned by Britain's Department for International Development. Its minister, Clare Short, believes that its £2 billion ($2.8 billion) budget should be spent purely on poverty alleviation. A publicly funded commercial enterprise, which seeks returns with no demonstrable impact on poverty, sits ill with her goal. The CDC offices in Uganda, Malawi, Ghana and maybe Mozambique—some of the countries the department is most concerned about—are to be closed. Of the four regions that the CDC now invests in, Africa, the poorest, comes bottom of the list for any new investments.

If the CDC acts as a pioneer, encouraging others to follow, that is fine. Lord Cairns insists that if it is able "to achieve its mission of realising attractive returns to shareholders, this will also have the effect of assisting social development." Yet the new investments are in urban services for the rich minority, and not in poor, rural areas where 85% of Africans live.

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China's housing market

Sticky as treacle

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If Chinese homes changed hands more often, the economy would benefit

IMAGINE one in ten Chinese moving homes every year, as their counterparts do in the West. Think of the spending power that this would unleash—billions of dollars in personal savings put to more productive use in furnishing and decorating homes, as well as driving new construction. With an economy held back by depressed consumer demand, the desire of tens of millions of Chinese to move into—and own—bigger and better homes could help to fuel growth.

Reuters

Looking at life on the fourth ring-road

That, at least, was the hope after the government's decision in late 1999 to lift a ban on the resale of privatised public housing—the kind of housing occupied by most city dwellers. But the hope has been only partly fulfilled. The home-furnishing market is indeed booming, but properties are not changing hands as much as had been expected. Tens of millions of people may long to buy their first homes, but prices even for tiny flats in run-down, socialist blocks, or for draughty brick bungalows in back alleys, are high—often little less than newly built accommodation.

Plenty of new buildings are going up. Local governments, along with quasi-private firms, are investing billions of dollars in housing construction. Officials reckon that, since the late 1990s, the housing industry has been contributing about 1.5 percentage points to annual GDP growth (which last year was 8%). The current five-year plan calls for the average area occupied by urban residents to increase from 13.6 to 23 square metres by 2005. That will mean a lot of building.

So what of the older homes? Only five years ago, these were owned mostly by state entities and allocated to employees by their *danwei* or "work unit", usually for a peppercorn rent. In the 1990s, the government took a bound towards creating a nation of homeowners by promoting the sale of this housing to occupants at a steep discount. But it would not allow the new owners to sell their properties: they might, heaven forbid, turn a profit. In 1999 it relaxed the rules to permit resales, as long as the work unit agreed.

That was an essential move if there was ever to be a healthy property market. By the late 1990s, estate agencies—not a few of them run by scoundrels—were beginning to proliferate in Chinese cities. Not only are millions of Chinese from the countryside anxious to gain a foothold in the cities; millions of urban folk are also eager to leave overcrowded family homes or to move closer to their work. For a whole new class of young professionals, flat-buying is a main dinner-table topic.

Yet from November 1999 (when restrictions on second-hand house sales in Beijing were lifted) to the end of last year, only 1,200 such homes changed hands in the capital. This is just over one in 1,000 of the once-public homes that were sold to their occupants under the housing reforms of the late 1990s. Wang Chengqing, a professor at the Chinese Academy of Social Sciences (CASS), says the sellers are usually the relatively rich, who can afford to move into newly built accommodation, or the corrupt, who have secured more than their entitlement from their *danwei*.

There are big deterrents to selling, not least many fees, taxes and bureaucratic hurdles. The seller of a typical 60 square-metre apartment in central Beijing, priced at 6,500 yuan ($760) a square metre, would have to pay roughly 57,000 yuan in various charges, about 15% of the selling price. If the seller wanted to move into newly built accommodation, the money left would be enough only for a similar-sized flat on the city's outskirts. That is not an attractive prospect, given the city's congested roads and awful public transport.

And then there are the *danwei*. Many are still reluctant to let their employees sell their homes, because of disputes over who is entitled to what. There are many employees who never received their fair share of housing and should now be given cash instead. But they are not getting that either, because their employers cannot afford it. Those with permission to sell might calculate that it is worth hanging on to their properties until a rich developer buys them out and razes the building.

An official from the construction ministry, quoted by the *China Economic Times*, says that if 10% of homeowners were to sell every year, and to spend an average of 100,000 yuan to buy and fix up their new properties (with the help of a fast-developing mortgage industry), this could pump nearly 1 trillion yuan into the economy. It would also speed up the movement of labour around the country. Mr Wang from CASS says that there won't be such a turnover for another decade.

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Economics Focus

The PC crowd

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A look at the economics of political correctness

IT HAS been a source of prudishness over the past two decades, and the butt of innumerable jokes: but why did political correctness arise in the first place? Stephen Morris, an economist at Yale University, thinks he knows the answer. His analysis* suggests that, from the point of view of its practitioners, political correctness is an entirely rational form of behaviour—although from a broader perspective, it is potentially wasteful. Either way, its days as a social phenomenon may be numbered.

The first part of Mr Morris's theory is best explained by means of a hypothetical situation. Suppose an adviser has what he thinks is valuable information to convey to a policymaker. The adviser is concerned to get the policymaker to heed his advice, but also to make sure that he is seen in a good light in future. If the adviser is not well-known, these two goals could promote perverse behaviour.

As a setting, Mr Morris uses a simplified version of America's debate about affirmative action. An adviser who recommends affirmative action would never be perceived as being racist, yet one who does not might be. Consider an adviser who does not support affirmative action, but is not racist: he might pretend to support affirmative action, even though it is against his beliefs. He wants, after all, to be a trusted voice in future debates. Even the slightest hint of racism could thus harm his future interests.

The same rationale can be applied to everyday manifestations of political correctness: in language, for example. Instead of saying "chairman", when the incumbent is a woman, somebody who is not a sexist might say "chair" or "chairperson", in order to avoid even the perception of sexism. Saying "chairman" might not automatically provoke charges of sexism, but it will increase the odds that one is perceived as sexist. For non-sexists, therefore, it is a practice worth avoiding purely in order to preserve their future effectiveness.

This comes at a cost. To use politically correct language, although not dishonest, can involve an uncomfortable change in behaviour. Still, the costs are smaller than when useful information is lost.

Mr Morris creates a model in which the adviser and policymaker interact repeatedly. Over time, the policymaker can begin to corroborate any suspicions of bias. The model assumes that an unbiased adviser cannot easily certify that he is not racist, and thus needs to forge a reputation. But by the same token, a biased adviser could build a false reputation by pretending to be something he is not. The higher the value of reputation—ie, the more important that future decisions are to the adviser—the more these effects will develop. Both types of adviser, the biased and the unbiased, would lie (or pretend) more often.

In the extreme, the policymaker would then be helpless to distinguish between biased and unbiased advisers. But the more important the early decisions, the more an adviser is likely to show his true colours. With a high opportunity cost to building reputation, both the biased and unbiased are less likely to play against type.

Mr Morris's model does not necessarily imply that political correctness makes society worse off. Anything that results in more unbiased information being passed from advisers to policymakers adds to the success of their interaction. So when a biased adviser masquerades as unbiased, welfare can be improved.

In the long run, the policymaker learns about his or her adviser's type. A biased adviser has no incentive to dissemble in the final round of a repeated interaction. So the more accurately a policymaker can distinguish between types of adviser, the more likely it is that he (or she) will be able to ignore biased advice. Still, because the unbiased adviser has an incentive to lie—to recommend in favour of affirmative

action even if he believes it is harmful—then the net effect on welfare is less clear.

Mr Morris's model suggests that the incentive to be politically correct fades as society's population of racists, to take his example, falls. With few racists about, actions that could be consistent with racism—such as advising against affirmative action—might not produce a racist reputation. This will be especially true when individuals and institutions behave elsewhere in such a way as to build their reputation. This newspaper, with luck, has a sufficiently liberal reputation to avoid charges of sexism when it uses terms such as "congressmen" and "businessmen" to refer to mixed-sex groups.

It would be wrong, however, to conclude that political correctness in America and Europe arose because racism or sexism increased. Rather, because these became socially less acceptable, the costs of racism or sexism increased for anybody who hoped to be taken seriously by society. A popular revival of these social ills would eliminate political correctness as surely as their disappearance.

Mr Morris points out that political correctness does not exist merely by dint of society's more egalitarian leanings. His theory does not need to be confined to standard PC notions related to race, gender or sexual preference. People might also lie, for instance, about their support for better economic relations with Cuba, or for universal health insurance, for fear of being tarred as a dangerous leftist. Here Mr Morris is emphatic: in his model, the advisers who adopt political correctness to avoid such slurs do not abhor the slur itself. They fear only the consequences for their future effectiveness.

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*"Political Correctness", by Stephen Morris. Journal of Political Economy, April 2001.

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Swap futures

Battle for a benchmark

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A new financial instrument in London aims to get even with Frankfurt

LONDON'S financial-futures exchange, Liffe, and the German/Swiss futures exchange, Eurex, are squaring up for yet another fight over competing futures contracts. Three years ago Eurex won the battle for the "Bund", the ten-year German government futures contract, because it offered cheaper, more efficient electronic trading (Liffe was then still an open-outcry exchange). For seven years the two exchanges had traded rival contracts, but when it was clear that Eurex had won, trading in London suddenly dried up, and all the volume went to Frankfurt.

Now Liffe wants to hit back with a new, not-so-secret weapon called the "Swapnote". It is a future not on bonds, but on euro interest-rate swaps. Liffe argues that swaps, which are bilateral agreements to swap types and maturities of interest payments, are a huge and growing market. Government-bond markets are shrinking, both in America and Europe. This week the volume of corporate and other non-government bonds denominated in sterling exceeded that of gilts (British government bonds) for the first time.

Another problem with bonds is their fragmentation. A dozen government-bond markets are denominated in euros. They have the same interest-rate fundamentals, yet many differences in credit, liquidity, trading patterns and so on. Swaps provide a better benchmark for interest rates of all maturities. The seizing-up of world bond markets after Russia's default in August 1998 showed how bond issues can suffer sudden illiquidity. Those caught with short bond positions can get squeezed.

Some bond traders are still smarting from losses in March, when there was a squeeze on Eurex's five-year bond contract, the "Bobl". Dealers could not find the right bonds with which to close their short futures positions. Eurex has since eased the rules on bond delivery and softened its fines for failing to deliver on time.

More by luck than judgment, Liffe also launched the Swapnote in March. Swapnotes are swap futures denominated in two-, five- and ten-year maturities. Volumes have been rising, partly because swaps cannot be squeezed in the same way as bonds. Average daily trading has reached around 25,000 contracts, and open interest (the measure of open positions being run by traders) is about 95,000 contracts, worth a notional *euro*9.5 billion ($8 billion). To put this into perspective, Eurex's ten-year Bund contract averages 500,000 contracts a day (*euro*50 trillion), with *euro*90 billion in open interest.

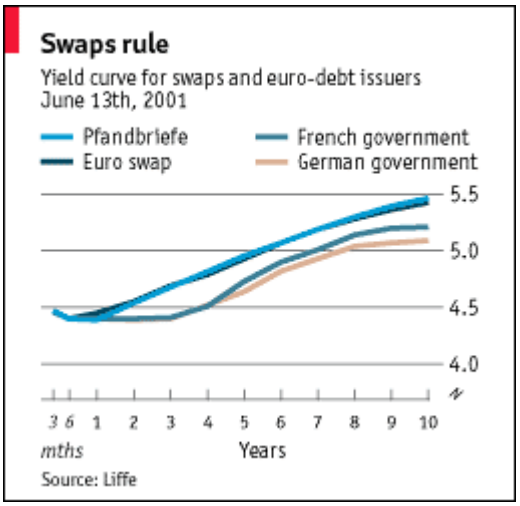
There are believers, though, or perhaps gamblers, who think that one day swaps will be the leading benchmark, with the Swapnote becoming the benchmark future. Liffe launched a similar product, too early, in October 1998. This time it has sought the backing of the most active swap broker, Garban-Intercapital, which has the copyright on the Swapnote name. Garban's boss, Michael Spencer, believes that exchanges and brokers are in the same business: providing pools of liquidity. He may even be seeking to make their roles indistinguishable, by merging Garban with Liffe, in which it has built up a 4.5% stake.

Mr Spencer has his fingers in several pies, including Blackbird, in which Garban has a 19% stake. Blackbird is an electronic swap-trading system that has been working since 1999, though it will not divulge its trading volumes. It recently formed an alliance to allow users to trade Eurodollar futures on the Chicago Mercantile Exchange, as well as swaps, through the Blackbird platform. Around 80 swap houses subscribe to Blackbird, though few admit to using it much. Even so, some think it may revolutionise swap trading, by further narrowing bid-offer spreads.

The big swap houses—the top commercial and investment banks—are developing their own secret weapon, SwapsWire, which will render electronic all the clunky parts of swap trading, such as documentation and settlement, without being a trading platform. (Because swaps involve two-way credit exposure, they will always be more complex than a bond or other commodity.)

As for Swapnote, it is a cash-settled bet on swap prices that are fixed daily by the International Swaps and Derivatives Association. This means that it has the price characteristics of a swap, without the two-way credit complexity.

So why might it not fly? The big swap houses say that swaps themselves are more flexible and can be designed to match exactly the cashflows of bonds. The trouble with Swapnotes is that they work to quarterly start dates. Still, the houses see a need for a futures instrument that tracks corporate-bond and German-mortgage bond (*Pfandbrief*) rates more closely than do the government-bond futures traded on Eurex (swaps are closer to non-government than to government bond rates—see chart). Eurex tried with a *Pfandbrief* future in 1998, but failed. The newly crafted Swapnote could possibly be the answer.



The rivalry is intense, even personal. Eurex wrested away Liffe's biggest contract, the Bund, now the world's most liquid futures contract. There is talk that Eurex is looking for a response to Swapnote. A mischievous Mr Spencer is busy guessing what Eurex will call it (SwapBobl? SwapBund?) and copyrighting the names.

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Financial regulation in Europe

Labouring with Lamfalussy

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The City of London is unhappy with two proposed EU directives

WHEN Alexandre Lamfalussy published his recommendations for the regulation of European securities markets last February, his report was praised by London's bankers and regulators alike. Few argued with the need to harmonise capital-market rules in Europe, and Mr Lamfalussy and his "committee of wise men" had come up with what seemed to be a sensible proposal to speed up the European Commission's action plan for financial services, by streamlining the legislative process. Yet the constructive mood has not lasted: the first two directives planned to follow the Lamfalussy procedure were panned this week by City types.

Why? Financiers claim that they had little say in drafting the two directives, despite the insistence of the Lamfalussy report on the need for consultation with market participants. (The commission and securities regulators protest, though, that they gave critics ample opportunity to comment.) The first directive aims to curb market abuse, namely insider-dealing (using information that is not public, to their own or others' advantage) and market manipulation (distorting the price-setting mechanism of financial instruments or spreading misleading information). The second directive deals with prospectuses, documents that help investors to assess issuers trying to raise capital or to have their securities traded.

When pressed, the critics admit that they support the idea of a single, universally valid prospectus for issuers, even if they dislike some of the directive's details. They are angrier about the market-abuse directive, which they say is too broadly phrased and covers too wide a range of markets and products. It states, for instance, that "member states shall prohibit any natural or legal person who possesses inside information from taking advantage of that information by acquiring or disposing of for his own account or for the account of a third party, either directly or indirectly, financial instruments to which that information relates." This, says John Serocold at the London Investment Banking Association, would, in effect, put securities analysts out of a job.

Yet it is natural for directives to be broadly phrased, since they are supposed to state principles; the fine details are firmed up later. There is, too, a strong case for stricter rules on market abuse, and for separating supervisory bodies from the markets they regulate. "Policing in Europe is still too lax, in particular compared with America," argues Karel Lannoo at the Centre for European Policy Studies in Brussels.

The question now is whether the two directives will make it through the new, streamlined process. Under the Lamfalussy rules, there will be only one reading in the European Parliament; the Council of Ministers will propose changes and secondary legislation will be left to the securities committee and the regulators' committee, the two new bodies proposed by Mr Lamfalussy. Yet if European parliamentarians reject the directives, they will have to go through the old, more cumbersome legislative process. Thus critics of the drafts have two options: either they can lobby finance ministers to get amendments through the council, or, perhaps more pleasurably, they can take Euro-MPs out to lunch.

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Tax evasion

Washing whiter

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French business grandees have been questioned over tax evasion

ARE the mighty fallen? No, but several barons of French business may feel they are being dragged towards a judicial abyss. This week it emerged that Claude Bébéar, chairman of the supervisory board of Axa, Europe's largest insurance company, and Henri de Castries, Axa's chief executive, had been called in by French police for questioning over tax evasion involving a Luxembourg insurer, PanEuroLife.

Embarrassing enough, given that Mr Bébéar is widely seen as both brilliant and virtuous—hence, now that he is in semi-retirement at the age of 65, his position as president of Paris's bid for the 2008 Olympics. Embarrassing, too, in that Mr de Castries, at 46, is just the sort of modern-minded internationalist that French business schools might choose as a role model for their students.

There is more to come. Even as Messrs Bébéar and de Castries were being questioned, so too was Jean Peyrelevade, now head of Crédit Lyonnais but formerly boss of UAP, a French insurance company which had a majority share in PanEuroLife and was taken over by Axa in 1996. All three are now part of an inquiry that began almost three years ago into allegations that PanEuroLife, headed by Gaston Thorn, a Luxembourger who was once president of the European Commission, used its life-insurance policies to allow small businessmen in France to avoid their taxes and launder money earned "on the black". "This normal procedure is aimed at shedding light on suspicions of money-laundering at PanEuroLife" said Axa of the questioning, as its share price fell sharply.

Also being investigated is Alain Gomez, the former boss of Thomson-CSF (now renamed Thales), a former arms and electronics group. Mr Gomez, a business star for most of the 1980s and 1990s, was taken into custody this week after a complaint by Lagardère, a competitor to the state-owned Thomson, that he had sought by underhand, nay, illegal, methods to undermine Lagardère. This resulted in Lagardère being the subject of a judicial inquiry, following which it was absolved. That gave its boss, Jean-Luc Lagardère, the opportunity to counter-attack.

Will there be more scandals, justified or otherwise, to embarrass the French elite? Certainly. France's independent magistrates, taking a cue from their Italian counterparts in the 1990s, increasingly enjoy wielding their enormous powers. The deeper reason is the culture of cronyism (and high taxes) that permeated politics and business under President Mitterrand. When top civil servants and businessmen come from the same top schools and swop the top jobs among themselves, a few corners get cut. Witness the scandal over Elf, the former state oil company, which has ended in jail sentences for, among others, Loïk Le Floch-Prigent, once head of France's railways, and Roland Dumas, once its foreign minister.

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China and the WTO

Edging closer

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A deal with America brings China closer to WTO membership (again)

ONE of the most protracted of all international diplomatic marathons may at last be near its finishing line. By reaching agreement with America on the terms of its accession to the World Trade Organisation, China has won a chance of joining the WTO this year. It may even meet the latest of many deadlines that have slipped by during the 15-year haggle: November, when the WTO's ministerial meeting in Qatar will mark a renewed attempt to launch a new round of world trade talks. Foot-sore marathon-runners, however, could be forgiven a weary feeling that China has passed this milestone before.

This latest deal came as a nice surprise after a grim few months in Sino-American relations. It was reached early on June 9th in Shanghai, in the margins of a meeting of the Asia-Pacific Economic Co-operation forum, and represented a triumph for the new American trade representative, Robert Zoellick. China had concluded a bilateral deal with America on its WTO accession in 1999. But several problems were unresolved. In Shanghai, China agreed to phase out rules curtailing American firms' access to the markets for reinsurance and big-ticket property insurance; a consensus was reached on limits to the spread of American retailers in China; and China agreed to lift restrictions on foreign companies' rights to import and export.

The biggest sticking-point, however, concerned China's market for agricultural products. America had insisted that China limit subsidies available to farmers to 5% of the value of agricultural output, in line with WTO rules for industrialised countries. It argues that China is too large to be accorded the privileges and exemptions that other poor countries enjoy. China has always wanted the benefits of developing-country status, including the right to subsidise agriculture up to the level of 10% of output. The compromise was to allow China some exemption, while extracting a commitment not to offer big financial incentives to farmers for particular crops.

The disagreement was partly symbolic—China's agricultural subsidies at present amount to only about 2% of output, and it would be hard-pressed to afford more. But it also reflected China's fear of the social and economic disruption that WTO membership may bring.

The agreement in Shanghai will allow America to support China at the next meeting (the 16th) of the WTO's working group on its accession, which is due to convene in Geneva on June 28th. But there is still more to do. The drafting and negotiation of accession protocols will take months. Other bilateral obstacles remain.

One WTO member, Mexico, has yet to agree the necessary bilateral deal at all. And there are outstanding disagreements with others, such as the EU, which has accused China of backtracking on promises to open its insurance market. Like America, the EU thought it had completed its negotiations with China. Here is the real threat to China's meeting its latest deadline for WTO accession: that, once again, its negotiating partners discover it does not share their idea of what has been agreed.

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Climate change

Burning Bush

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A new report from America's National Academy of Sciences confirms the reality of global warming

Get article background

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To defuse the rows over these two dropped bricks, the Bush team promised to come up with a credible alternative policy that was more than mere Kyoto-bashing. And to help form that policy it called, on May 11th, on the services of the National Academy of Sciences (NAS) to provide guidance on the matter as soon as possible. America's most prestigious scientific body hastily organised an expert panel under the chairmanship of Ralph Cicerone of the University of California, Irvine, to meet that request, and the results of its deliberations have just been released. The first paragraph of the report says it all:

> Greenhouse gases are accumulating in Earth's atmosphere as a result of human activities, causing surface air temperatures and subsurface ocean temperatures to rise. Temperatures are, in fact, rising. The changes observed over the last several decades are likely mostly due to human activities, but we cannot rule out that some significant part of these changes are also a reflection of natural variability. Human-induced warming and associated sea level rises are expected to continue through the 21st century.

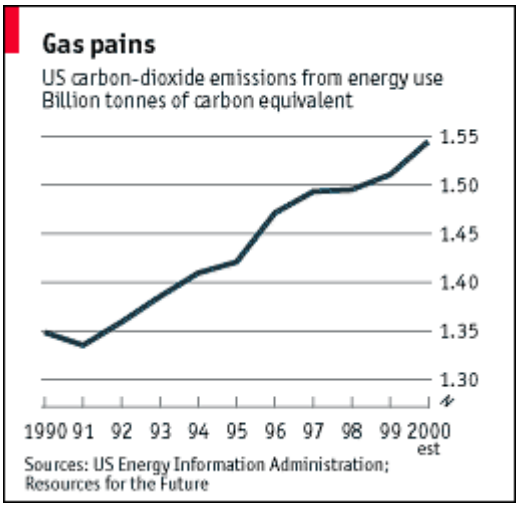
Now will you believe it?

The NAS's conclusions, which include no new data, will come as no surprise to those working in the field. They more or less confirm a recent report from the United Nations' Inter-governmental Panel on Climate Change (IPCC) that laid out the scientific case for taking global warming seriously. What they do provide is political cover, if Mr Bush wishes to use it, for a graceful retreat. Many Americans were, for various reasons, unwilling to accept the authority of a UN-sponsored study. A home-grown one is not subject to any such political caveats.

The administration left itself remarkably little wiggle-room in the mandate that it gave Dr Cicerone. The panel was asked not only about the certainties and uncertainties surrounding the science of climate change, but also about the worth of the UN report and its conclusions. In particular, it was asked explicitly whether there were substantive differences between the IPCC's scientific reports (lengthy tomes detailing the state of climate science) and the summary for policymakers (which suggests that there is

enough scientific evidence to warrant action now). Critics of the Kyoto treaty have long argued that this summary can only have been the result of political sleight of hand.

That always looked unlikely. After all, the evidence was alarming enough as long ago as 1992 for Mr Bush's father to sign a UN treaty in Rio de Janeiro that was intended to fight global warming. This treaty is the framework for the Kyoto process. Since then, new evidence has confirmed that global warming should be taken seriously. The IPCC's summary report went so far as to declare that man's actions have contributed "substantially to the observed warming over the last 50 years". An earlier IPCC report had predicted that, if current trends continued, the temperature of the atmosphere could rise by 1.0-3.5°C by 2100; the latest one expanded the range of likely warming to 1.5-6.0°C.



This is not to say that no uncertainties remain. On the contrary, the NAS panel is frank about how much of the science is still hazy. In particular, its report highlights the role of aerosols (small, airborne and often man-made particles that reflect sunlight and thus cool the atmosphere, rather than warming it). It also comments on the inadequacy of existing computer models of climatic change, and the current lack of understanding of the feedback loops that influence the sensitivity of the climate to increases in greenhouse gases. Such feedback loops might slow any warming trend; but they might, on the other hand, accelerate it. And, although the NAS offers a likely temperature range for the next century that is slightly less alarming than the IPCC's, and it attaches more provisos and caveats to its conclusions than the UN panel did, it nevertheless leaves little doubt that global warming should be taken seriously.

Indeed, the NAS's endorsement of the UN panel is striking: "The IPCC's conclusion that most of the observed warming of the last 50 years is likely to have been due to the increase in greenhouse gas concentrations accurately reflects the current thinking of the scientific community on this issue...The full IPCC Working Group I report is an admirable summary of research activities in climate science, and the full report is adequately summarised in the Technical Summary."

The NAS also rejects the insinuation, apparent in the questions from Mr Bush's team, that the UN process was politically manipulated. It is true, it explains, that the IPCC summary "reflects less emphasis on communicating the basis for uncertainty and a stronger emphasis on areas of major concern associated with human-induced climate change." However, rather than blaming some socialist skulduggery, the authors suggest that this "change in emphasis appears to be the result of a summary process in which scientists work with policy makers." It notes that no changes were made without the consent of the IPCC's lead authors, and opines that most of the changes that did occur "lacked significant impact."

The result is bad news for those who had hoped for a rejection of the IPCC's conclusions. And, though the sceptics on the NAS panel itself have rushed to make it clear that their report does not, in any way, endorse Kyoto, that is largely because the report offers no views whatsoever on any policy options. Nobody who takes this report seriously can easily argue for doing nothing.

What Mr Bush himself will do is not yet clear. He has accepted the results of the study, and acknowledged the report's chief conclusion that global warming is real and at least partly man-made. And, though he has once again rejected the Kyoto pact as "fatally flawed", he has also accepted that an international, UN-led approach is the right way to deal with this most global of problems.

However, he has yet to offer any credible alternative to the Kyoto deal. His immediate response this week was to offer to spend more government money on climate science and greenhouse gas-related technology. Those are certainly worthy causes, but they do not address the central point. A bigger plan is needed, and it would be politically convenient if at least its outlines were clear within the next few weeks. The next round of talks on the UN pact are scheduled for July in Bonn. If the Americans have nothing to offer by then, they will run into a lot more criticism.

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Climate change

Burning Bush

Jun 14th 2001
From The Economist print edition

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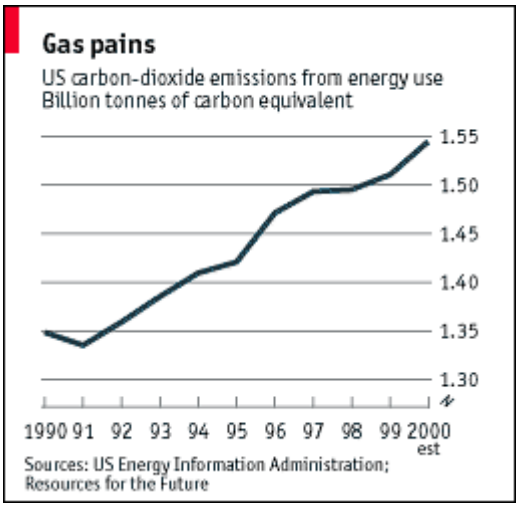

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Science and technology correspondent

Jun 14th 2001
From The Economist print edition

The Economist is looking for a new science and technology correspondent. The job is based in London. Applicants need not necessarily have journalistic experience, but they must possess a clear and witty writing style and a wide-ranging knowledge of, and enthusiasm for, the subjects. Applications should include an article suitable for publication, and should be e-mailed to scijob@economist.com. The closing date is July 7th.

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Condensation in aircraft

The rain in planes

Jun 14th 2001
From The Economist print edition

Jetliners suffer from too much moisture and their passengers from too little

SINCE people are made largely of water, transporting 350 of them thousands of kilometres through the air in a metal canister is a sweaty business. On average, each person on board a commercial airliner gives off 100ml of moisture every hour. That means a jumbo collects some 600 litres during a 17-hour transpacific flight, much of it as condensation in the gap between the cold outer skin of the aircraft and the insulated cabin wall. Meanwhile, the people who have sweated off this moisture are being tortured by a cabin atmosphere that is too dry. Its relative humidity is around 20%. Comfort demands a figure nearer 40%.

CTT Systems, a Swedish company founded ten years ago by two Saab aircraft mechanics, sees an arbitrage opportunity in these two facts. By adapting some 70-year-old Swedish air-conditioning technology, it has created a system that dries the air in the cavity between the hull and the cabin walls, while keeping the cabin itself comfortably moist.

CTT's Zonal Drying System takes the moist air leaving the cabin and feeds it through a rotor impregnated with silica gel. This removes the moisture. The dry air is then blown between the cabin wall and the aircraft's skin, absorbing any condensation that has formed there. Then, a stream of warm air is run through the rotor unit in the opposite direction. This absorbs the moisture from the silica gel and feeds it back into the cabin whence it came, keeping the passengers comfortable.

Passenger comfort is important, of course. But condensation in the gap between cabin and hull can be lethal. This gap contains much of an aircraft's wiring, and water can damage that wiring's insulation. Such a problem is thought to have contributed to the loss of a Swissair DC-11 off the Atlantic coast of America a few years ago. Too much condensation causes other difficulties, as well. There have been cases when ice has built up inside the tailplanes of aircraft, causing their rudders to freeze and thus preventing their pilots from steering them.

There is also the matter of weight. An aircraft such as a Boeing 747-400 can accumulate as much as 700kg of condensation before it reaches equilibrium. Even though that is only about 0.17% of the 400 tonnes such an aircraft weighs fully laden, it is enough to cause problems for the pilot when he tries to trim the balance of the aircraft. And 700kg is about the weight of nine men. So the aircraft is carrying the equivalent of at least nine non-fare-paying passengers, in an industry where every extra kilogram affects fuel consumption and profit margins.

So far, CTT Zonal Drying Systems have been installed by Swissair, KLM and Lufthansa, to deal with specific dampness problems in particular aircraft in their fleets. This costs between $40,000 and $120,000, depending on the size of the aircraft. Now, Airbus Industrie is planning to build the moisture arbitrageurs in at the factory. It will offer the Zonal Drying System as an optional extra on its long-haul A330 and A340 models.

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Computer viruses

The good, the bad and the ugly

Jun 14th 2001
From The Economist print edition

Can computer viruses ever be a force for progress?

IN THE wild west of the online world, the archetypal baddies are computer viruses and worms. These self-replicating programs are notorious for wreaking havoc in the systems of unwary users. But, as in the west, not all gunslingers wear black hats. Some virus writers wish their fellow users well, and have been spreading viruses that are designed to do good, not harm.

Cheese Worm, which appeared a few weeks ago, attempts to fix computers that have been compromised by the Lion Worm. The Lion Worm is dangerous. It infects computers that use the Linux operating system, and creates multiple "backdoors" into the infected computer. It then e-mails information about these backdoors to people who wish to misuse that computer for nefarious purposes such as "denial of service" attacks on websites. (Such attacks bombard a site with so many simultaneous requests for access that it comes out with its hands up.)

That might sound like a good thing. So might VBS.Noped.A@mm. This virus, which arrives as an e-mail attachment, searches a user's hard drive for specific files which the (unknown) virus writer believes contain child pornography. If the virus finds any files on the proscribed list, it e-mails a copy of the file in question to a random recipient from a list of American government agencies, with an explanatory note.

The notion of "good" viruses may sound novel; but, according to Vesselin Bontchev, a virus expert with Frisk Software International in Iceland, it is not. However, early attempts to create beneficial viruses—for example, programs that compressed or encrypted files without asking a user's permission—were resented, because they represented a loss of control over a user's computer, and a diversion of data-processing resources. Inoculating computers against infection sounds like a good idea, but fails because any unauthorised changes are suspicious.

Cheese Worm, even though it is designed to help the user whose disk it ends up on, suffers from the same objection. And VBS.Noped.A@mm, whatever social benefits its author might think it has, is not even meant to do that. If it works, it will harm the user rather than help him. It is little more than cyber-vigilantism. Appropriate to the wild west, perhaps, but if cyberspace is to be civilised, other solutions will have to be found.

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Cities and commercial life

Location, location, location

Jun 14th 2001
From The Economist print edition

Mary Evans

Why place still matters

IT IS one of the ironies of the age. Just as the wonders of communications technology make it possible to conduct all sorts of computer-based activities from any corner of the earth, so humanity clusters more into cities than ever before. Location, which should surely be irrelevant, seems to matter more, not less. Physical proximity appears to have virtues in commercial life that no amount of technological gimmickry can replace.

No better example exists of the enduring importance of place than the City of London, still (despite all its tribulations) the world's largest international financial centre. Yet the riddle that emerges from the fourth volume of David Kynaston's delicious history of the City is that location has continued to matter even after so many of the City's physical contacts have disappeared. No longer do bankers sit over lengthy lunches, or jobbers josh on the floor of the Stock Exchange, or top-hatted discount brokers drop round at the Bank of England each afternoon.

Much of what made the City look like a village has gone too: the little alleyways have disappeared under tower blocks. Some of the biggest banks have defected to Canary Wharf, a taxi ride away. Back in 1960 Durlachers, then a stock-jobbing firm, moved to Austral House, ten minutes from the Bank of England and the Stock Exchange. "People thought we were mad," recalled one senior figure, "because nobody thought that anybody could operate at that vast distance."

With the disappearance of village life have gone many of the City's most colourful figures, vividly depicted by Mr Kynaston. The working day has grown, and the screen has replaced the trading floor. The incoming American banks have supplied a few figures of their own, such as Larry Becerra, king of the proprietary traders at Goldman Sachs in the late 1980s, who rode to work on a Harley-Davidson and told one floor trader who asked how much of a certain security to acquire, "Buy them till your hands bleed." Sociologically the City has changed too. In the 1960s Jocelyn Hambro, the head of another now-vanished merchant bank, pursued a recruitment policy based on what he termed "enlightened nepotism": on a genealogical chart pinned up in the bank's dealing room, the names of unmarried and eligible female Hambros were helpfully underlined in red.

The atmosphere of the village, where everybody knew (and had probably been

The City of London (Volume IV): A Club No More, 1945–2000
By David Kynaston

Chatto & Windus; 896 pages; £30

Buy it at
Amazon.co.uk

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Buy it at
Amazon.co.uk

Airspaces
By David Pascoe

Reaktion Books; 304 pages; $27 and £17.95

Buy it at
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Amazon.co.uk

to Eton with) everybody else allowed financial regulation to be an informal matter of Etonian codes of honour. It also caused the City to resist, in the first couple of decades after the second world war, the influence of outsiders. Coupled with a fixation on the importance of sterling as an international reserve currency, it made the City establishment slow to appreciate the emergence of global financial markets, starting with that for the Eurodollar.

regulation was once merely a matter of Etonian codes of honour

The recent history of the City has been dominated by two big trends: the move from informal to formal financial regulation, and London's re-emergence as an international financial centre, as powerful and prosperous as it was before 1914. The move to formal regulation was driven by a series of home-grown City scandals, from the debacle at Lloyd's to the destruction of the ancient house of Barings by Nick Leeson's speculations. The revival of London as the premier international financial centre has been largely the work of foreign houses, which began to pour into London in the 1970s, and in the 1980s swallowed most of the grand old names.

Why did the foreigners come? Why to London? Why not to Paris or Frankfurt? That is a question that Mr Kynaston, for all his immense skill in weaving analysis with telling anecdote, never really addresses. There is a hint of the answer in an essay by Saskia Sassen, a professor of sociology at Chicago University, in the collection of essays edited by Allen Scott. She argues that the emergence of the "global city" (she has written a book with that name) is mainly a result of the growing complexity of big corporations, as their operations become dispersed around the globe. In the face of mounting intricacies of co-ordination and control, companies increasingly outsource central functions to specialised service firms.

Such specialised firms—in law, accounting, finance and so on—need to draw on a huge pool of talent, expertise and information, most readily found in large cities. "Global cities are, in this regard, production sites for the leading information industries of our time," she explains.

In the case of London, an essay by Sir Peter Hall, a British geographer, argues that there is strength in depth. New York's largest law firms, for instance, are more represented there than in any foreign city; in a range of other activities, from advertising to accountancy, firms around the world are more likely to have a branch in London than elsewhere. Strength in depth, together with English and the ability to extend the working day into the two other main time zones, may be London's big advantage as a world city.

So location matters. But, for those who staff the global service industries, location is a new sort of concept. Its strange quality is captured in David Pascoe's maddening book. Airspaces, it seems, are what exists above and around airports. His premise, he announces, is that "it is not simply through the basic physical manifestations of airspace that we can discern the shapes of our modernities; we must be aware of its representations."

If you don't understand that, you won't make head or tail of the rest of the book, but you will enjoy a trip around the poetry, cinema, architecture, literature and history of airports and aviation, from Proust to Andy Warhol, together with a charming photograph of the celebration of Midnight Mass at Paris's Orly in 1966. The scope of Mr Pascoe's rumination is impressive, and includes air terrorism, air accidents and airport seat design—just the thing for that banker stuck in the departure lounge at Heathrow's terminal four, wishing that distance were truly dead.

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Understanding the sky

Atmospheric stuff

Jun 14th 2001
From The Economist print edition

There is still a lot about the sky that we don't know

"WHEN two Englishmen meet", noted Samuel Johnson, "their first talk is of the weather; they are in haste to tell each other, what they must already know, that it is hot or cold, bright or cloudy, windy or calm." The weather is easy to describe but hard to explain, let alone predict. But the first step towards understanding is often naming and categorising, so that meaningful patterns can be identified; and the man who defined the language with which to describe the face of the sky was an Englishman called Luke Howard. In 1802 Howard, an unknown amateur scientist, gave a lecture in which he named and defined the different types of cloud—cirrus, cumulus, stratus and their various hybrid forms. The value of Howard's cloud taxonomy was recognised immediately, since it gave scientists a standardised way to record and compare observations and begin to form theories. As well as nailing down the clouds, Howard's new language of the skies inspired Constable to paint his studies of the skies over Hampstead, and prompted Goethe to compose a poem in Howard's honour. With a few minor modifications, his system is still in use today.

Not much is known about Howard, who was a modest and private man, so a book-length account of his improbable route to scientific renown is likely to include a broader view of the times. In "The Invention of Clouds", Richard Hamblyn gives a fascinating description of the late 18th-century vogue for science lectures as a form of popular entertainment, as well as excursions into the histories of ballooning, weather forecasting and scientific publishing. Appropriately enough at a time when the debate over the origin of species was warming up, Howard deliberately emphasised that his cloud categories were not fixed species, but dynamic "modifications". He thus opened the way for later theorists to use the changing clouds as visible indicators of invisible atmospheric processes. Howard's work also directly inspired Francis Beaufort, who created the standard scale for wind speeds.

It is fascinating stuff, though Mr Hamblyn's language is somewhat freighted with the political codewords and overwrought rhetorical flourishes of the cultural studies crowd, and at times some of his theorising (on the power-confirming nature of operatic cloud machines, for example) seems wholly speculative. Even so, his account of Howard's success in defining the apparently indefinable is lively and readable, and his book accomplishes that rare feat of changing the reader's perception of the world.

"The Northern Lights", Lucy Jago's biography of Kristian Birkeland, a Norwegian scientist who discovered the origins of the aurora borealis, is written with the sensibility of a novelist rather than an academic. Birkeland makes an amusing hero; he liked to wear a Fez and slippers in his laboratory, and paid for his research by developing an electro-magnetic gun and a process to turn the nitrogen in air into fertiliser, among other inventions. Having found lucrative industrial uses for his understanding of high-voltage physics, Birkeland spent the last years of his life pursuing whatever took his fancy, and ended up investigating the zodiacal light from Egypt and Sudan. But Birkeland also suffered from bouts of depression, and his work took a terrible toll. He was cheated of a Nobel prize by a business partner, and his auroral theories were disregarded in his lifetime.

Exhaustive research by Ms Jago, a former documentary producer, enables her to describe the scenes from Birkeland's life in apparently photographic detail. But her enthralling, novelistic descriptions are undermined by her author's note, in which she admits to "telescoping events in order to avoid the story

The Invention of Clouds: How an Amateur Meteorologist Forged the Language of the Skies
By Richard Hamblyn

Farrar, Straus and Giroux; $27
Picador; £14.99

Buy it at
Amazon.com
Amazon.co.uk

The Northern Lights: How One Man Sacrificed Love, Happiness and Sanity to Unlock the Secrets of Space
By Lucy Jago

Hamish Hamilton; 320 pages; £14.99. Knopf (October); $24

Buy it at
Amazon.com
Amazon.co.uk

Cambridge Encyclopedia of the Sun
By Kenneth R. Lang

Cambridge University Press; 280 pages; $49.95 and £29.95

Buy it at
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becoming too long" and making "assumptions that are not documented but are reasonable". This sort of thing is forgivable, even necessary, when making television programmes, but not in a history book; Ms Jago should perhaps have just written a novel. She could also have been a little more sceptical about some of Birkeland's more outlandish theories, which have not stood the test of time.

Both books examine areas in which scientific knowledge still contains obvious gaps. The processes of cloud formation and precipitation are still poorly understood, as is the extent of the sun's influence on terrestrial weather and climate, an uncertainty seized on by those still clinging to the belief that global warming is not predominantly caused by man.

Compared with physics and chemistry, in which superstition was banished long ago, beliefs that seem laughably primitive today were held until quite recently in both meteorology and solar physics, and both fields are now changing fast as a result of satellite technology. As Kenneth Lang writes in the preface of the "Cambridge Encyclopedia of the Sun", three spacecraft have provided more important new information about the sun in less than a decade than perhaps the entire century of previous observations. Despite the valuable work of researchers such as Howard and Birkeland, the science of understanding the changing complexion of the sky still awaits its Newton.

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Insects and disease

Little and lethal

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From The Economist print edition

Mosquito
By Michael D'Antonio and Andrew Spielman

Hyperion; 256 pages; $22.95. Faber and Faber; £10.99

Buy it at
Amazon.com
Amazon.co.uk

WEST NILE virus is a nasty disease that usually afflicts people in Africa and the Balkans. When an outbreak occurred in New York in 1999, the news reports were predictably apocalyptic. Nasty tropical ailments are not meant to reach the Upper West Side.

After a long career in tropical public health, Andrew Spielman has a rare and deep appreciation for the mosquito, a tiny insect that spreads not just West Nile virus, but also malaria, yellow fever, dengue, filariasis and the deadly encephalitis. Over the centuries the mosquito has killed many, including Alexander the Great and Oliver Cromwell, and worn down regimes as powerful as the Roman empire. The parasites it produces are particularly good at disguising themselves and at changing character, which is why so many modern anti-malarial medicines quickly become ineffectual. The mosquito, Mr Spielman says, has great staying power.

It walks on water and on land. It flies through the night with the aid of the stars. It sees and smells, and also senses heat from a distance. Lacking our kind of brain, it thinks with its skin, changing direction and fleeing danger in response to changes in air pressure. The mosquito, though, is a self-serving creature. It doesn't aerate the soil, like ants or worms. Nor is it an important pollinator of plants like the bee. It does not even serve as an essential food item for some other animal. It has no purpose other than to perpetuate its species, and for that the female needs blood. That some species of mosquito plague human beings to fulfil this need is, to the insect, incidental. The mosquito is simply surviving and reproducing. When Archy, Don Marquis's versifying philosopher cockroach, remarked that, "a man thinks he amounts to a lot, but to a mosquito a man is merely something to eat," he was closer to the truth than he knew.

Most books about mosquitoes are as deadly as the diseases spread by their subjects. "Mosquito" is a rare exception. Mr Spielman has a gift for detail—about *Opifex fuscus*, the mosquito rapist, or *Culex pipiens*, which is born with its sexual organs the wrong way round. He wears his scholarship lightly and his enthusiasm for his subject is endless. If you have never read a book on entomology, be sure to start with this one.

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18th-century caricature

James Gillray

Jun 14th 2001
From The Economist print edition

We admit we have an interest, as The Economist is providing financial support. But others should be interested too in James Gillray, and not just because one of England's finest caricaturists of the late 18th century had his studio at 27 St James's Street, part of our current address. His irreverent and often lewd views of the monarchy, William Pitt and Charles James Fox, the French revolution and high society are on show at Tate Britain in London until September 2nd.

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German fiction

Guns 'n' roses

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Three new novels that are full of mind games

THE most obvious translation of the title of Karin Reschke's novel, "SpielEnde" would be "end of the game" or simply "endgame". But, if the second "e" were written instead in lower case, the title could also mean "players". The double-take is wholly appropriate, for the book tells the story of a sinister game and its quite unpredictable participants.

Five friends arrive for a birthday celebration and find their hostess, the elderly Cornelia, shot dead, apparently by her own hand. The narrator, Feline, inseparable companion of the dead Cornelia, goes on a journey with her ashes and becomes involved in a series of bizarre adventures all directed by the dead woman whose influence on Feline is revealed to have been malign. Quite ruthlessly, step by step, Feline sets herself free.

The plot is so intriguing that it would be a crime to reveal the ending. The game is one of tyranny and revolt, of cruelty and revenge. The relationship between Cornelia and Feline replicates itself, like a cancer. But as spectators we remain at a little distance, intrigued but never deeply involved. In the past Feline has paid her way by writing sensational fiction, and she often reverts to that mode in the telling of her own story. One wonders, though, how convinced she is by her own fiction, and how seriously she intends it.

SpielEnde
By Karin Reschke

Ullstein Berlin; 176 pages; DM34

Buy it at
Amazon.de

Rosenfest
By Leander Scholz

Carl Hanser Verlag; 246 pages; DM35

Buy it at
Amazon.de

Hoffmann
By Peter HÃ¤rtling and Peter Härtling

Kiepenheuer-Witsch; 252 pages; DM38

Buy it at
Amazon.de

"Rosenfest" (Festival of roses) is Leander Scholz's first novel and is dedicated to its heroes, Andreas Baader and Gudrun Ensslin. Although he deals with real people and real events, Mr Scholz insists that this is a work of fiction. The book opens in 1967 with the killing by police of a student, Benno Ohnesorg, during a violent demonstration against the Shah of Iran. It ends with the arrests of Baader and Ensslin for their bombing of two Frankfurt department stores and of the Springer press in Hamburg.

As a writer of fiction, Mr Scholz conflates and rearranges, and his chief interest is in the love affair between the two idealistic terrorists. Fiction has trouble asserting itself against lives and times that are themselves so compellingly interesting. Mr Scholz does bravely, but you can feel him being pulled—and ourselves with him—into the fascination of realities; his book is weakest precisely in those places where he has had to strive to make things up. Thus Ensslin and Baader on holiday in the turbulent Paris of 1968 or in flowery Tuscany behave like many Germans romantically convinced that authentic life can only be lived outside the mother country. The idyll is not convincing. Mr Scholz revives an unhappy passage in Germany's recent history, and replays the inexorable machinery by which the state and its radical critics provoke one another into a terrible cul-de-sac. But surely readers can fairly ask that a novel do more than merely revive our interest in old debates. Fictions must achieve a life of their own, but Mr Scholz remains essentially parasitical on historical events that are intrinsically (and rarely) far more interesting.

Peter Härtling, however, is a master of the art of fictional biography. He has had successes with Hölderlin and Schubert. He calls this latest venture, whose subject is a writer and composer named E.T.A. Hoffmann, a "Romanze", a word nicely including music and literature as well as the love affair that is central to the story. Hoffmann was continually and variously in love—hence the subtitle: "manifold love"—but that was only one expression of his polyphonic character. In his composing, Mozart, Gluck and Beethoven intruded; in his writings he split himself and his lovers, friends and enemies again and again into contending voices.

In many of his stories the storyteller is himself one of the characters. Utterly convinced by the fiction he relates, his power over his audience is total. Mr Härtling's great achievement is to convey that exuberant and compelling polyphony, and even to augment it with a further voice, his own. For he is present as

biographer, going under the spell of his subject, and thus carrying the reader with him. The book is a delight—in turn, funny, passionate and heartbreaking from one unstable moment to the next.

As picaresque at times as Feline's adventures in "SpielEnde" and as engaged in social realities as Mr Scholz in "Rosenfest", in conviction Mr Härtling shows both writers the way.

His Hölderlin novel of 1976 emerged from the same context of radical and thwarted idealism that also produced Ensslin and Baader. His Hoffmann romance continues that radicalism, as the Romantic imagination pits itself against a repressive social order. Very often, in Hölderlin's life, for example, and here again in the love affair of Hoffmann and Julia Marc, marriage is a particularly revealing battleground. Julia is sold off to a "suitable" husband who later abuses her. Many years afterwards she recalls what Hoffman, a passionately married man himself, made of her in his imagination. Mr Härtling's Hoffmann has complete autonomy, and is all the more powerful for it in its assault on reality.

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Reading habits

Scribble, scribble

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CHARLES LAMB once confessed to such a "community of feeling with my countrymen" about Shakespeare's plays, that he preferred reading them in editions that had been "oftenest tumbled about and handled". It is with just this feeling that H.J. Jackson has written her book about marginalia. She concedes that there are those, like Virginia Woolf, who shudder at the "ohs" and "poohs" and "beautifuls" scribbled by choleric or sentimental readers. But such is Ms Jackson's "community of feeling" with readers that, whether the note is a simple "hello?" or a "mind that, John", or whether it is Keats on Milton, she is able to convince us that here is a rich resource for historians of reading.

Marginalia: Readers Writing in Books
By H.J. Jackson

Yale; 330 pages; $27.95 and £19.95

Buy it at
Amazon.com
Amazon.co.uk

In fact marginalia have a distinguished history, going back to the scholarly glosses and rubrics for which room was specially left in early manuscripts and, after them, in the first printed books. These impersonal, editorial annotations then came to be actually printed in the margins of books, with further space left for yet more manuscript additions. Commentary thus swarmed round the texts, almost on an equal footing with them. But in about 1700, an innovation took place—namely, the footnote. Commentary was demoted. This, Ms Jackson suggests, may have contributed to the evolution of the author as independent agent. What it also did was to leave the margins clear for a new kind of independent and interventionist reader.

It is really from the 18th century onwards, with the increase of middle-class book-buyers, that margin-scribblers begin to speak informally, in their own voices; and from then, too, that certain books (she chooses, for example, Boswell's "Life of Johnson") begin to attract the pencilled conversations of generations of argumentative readers. Here are the famous, the obscure and the anonymous, children, lovers and nutters, all of whom, for different reasons, have one thing in common: they must pitch in. "One longs to say something", wrote one prolific annotator, Hester Piozzi, the friend and benefactor of Dr Johnson. And such is the nature of the medium, that whatever is said comes across with time-defying directness: next to a sonorous phrase of Johnson's, for example, about the summer being "gloomy, frigid and ungenial", another contemporary has written furiously, "Why can't you say Cold like the rest of ye world?"

Writing in books is itself contentious, and Ms Jackson is interesting on the motives of marginal scribblers. Who is the addressee? Is it the author, so often addressed as "you", but who equally often may be dead? Is it the book itself, for its own good, so to speak? Or future readers, like sending a message in a bottle? Is it the note-taker him or herself? And how are marginalia, so close to the act of reading and so intimately next to the text, different from the reader's diary? Coleridge, the first writer to have his marginalia collected and published, was often asked by his friends to annotate their books; but it seems that behind this relatively public stance was a private process almost of self discovery: "A book", he wrote, "I value, I reason and quarrel with, as with myself when I am reasoning."

Ms Jackson wishes ostensibly to alert scholars and librarians to the importance of marginalia. But the warmth and humour of "Marginalia" reach beyond to the lay reader, who is often tempted to risk scholarly indignation and scribble in its pages, "how true".

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Rock music

Sigur's saga

Jun 14th 2001 | REYKJAVIK
From The Economist print edition

Once a home of Nordic bards, Iceland is now exporting rock bands

ICELAND'S capital defies its small size in most things, not least in culture. The 280,000 residents of Iceland's geyser-pitted capital enjoy five professional theatre troupes, a national opera and a contemporary dance company. But where Iceland really excels is in alternative rock music. Leading the way is Bjork, a pixie-diva whose quirky voice has made her the most famous Icelander alive—though at a cost: she has become too commercial for Reykjavik's hipsters. "I respect her," says one dreadlocked musician, "but I would never listen to her. Way too plastic."

Sigur Ros have a feel for landscape

Hljomalind is a grungy independent record store in downtown Reykjavik. Kristjan, the cheerful communist behind the counter, puts the strength of Icelandic music down to the fact everyone knows each other. "If something is good, word travels quickly." Friendly competition helps, as does the fact that most things—a new bass guitarist for instance—are only two phone calls away. A number of new Icelandic bands are promising to take over where the Sugar Cubes, Bjork's original band, left off. Young talent is recognised and supported at home, not by the government which, musicians complain, underwrites just about every other cultural endeavour, but by a progressive Icelandic label, Smekkleysa (Bad Taste), set up by Einar Orn, formerly of the Sugar Cubes. Three bands he has scouted stand out. For lovers of very loud noise, there is Minus, an experimental thrash band. A softer, more electronic sound comes from Mum. Then there is Sigur Ros, the hottest thing to come out of Iceland since, well, Bjork.

Sigur Ros have already captivated the music press on both sides of the Atlantic. The band's third album and first international release, "Agaetis Byrjun" (A Good Start), was the pick of many rock critics around the world last year. "The kind of beauty that could drive you to the brink of madness." Radiohead were so impressed they have twice asked the Icelanders to tour with them. Icelanders buy more CDs per capita than anyone else; 15,000 of them have bought "Agaetis Byrjun". "Even my parents listen to it," laments one fan.

Word of the band has reached America where, because the release has been delayed, "Agaetis Byrjun" has been bootlegged from the Internet, in record numbers. This, despite the fact that Sigur Ros sing either in Icelandic or in a language of their own making, "Hopelandic". No matter if audiences can't understand the words. "They get to make their own words and dreams," says the softly spoken lead singer, Jonsi Birgisson.

Only 25, Mr Birgisson has the makings of a superstar. He is something of a Viking anti-hero: slightly built, his locks shaven but for a spare Tintin-style quiff, blind in one eye, openly gay and (most scandalously for an Icelander) a vegetarian. His voice and guitar drive the band, who use conventional instruments in unconventional ways. Mr Birgisson attacks his guitar with a violin bow and sometimes sings directly into it, producing a dreamily distant sound. His exquisite countertenor voice serves as another instrument, while strings and keyboard produce something not far from whalesong.

Mr Birgisson, who is openly gay and sports a Tintin-style quiff, could pass for a Viking anti-hero

The industry categorises them as ambient rock or post-rock. Naysayers call their sound "elfin". Others find it angelic, heavenly, ethereal. No song on "Agaetis Byrjun" lasts less than seven minutes. Each begins slowly, drawing you in like the undertow of a wave, before crashing down on them. Mr Birgisson flinches when asked to expound on the music. "I don't know," he says finally, "just call it sincere."

Hailing from Iceland lends an exotic allure, but also invites labelling: snowpunks, icerockers, popsicles.

Still, Sigur Ros admit Iceland's landscape is an influence. The vistas from their studio outside Reykjavik are inspirational: cobalt ocean, snowy mountains, black lava rimming a valley of bright green grass like eyeliner. Sigur Ros's connection with the Icelandic language runs similarly deep. They have no plans to release an album in English. Their next effort will be a collaboration with an Icelandic farmer who chants lyrics in a traditional fashion.

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Literary criticism

Dead wrong

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STANLEY FISH, now at the University of Illinois in Chicago, is probably the most eminent provocateur in America's Eng-Lit establishment, chided for all manner of intellectual sin from relativism to political correctness. He is also, more pertinently, its most famous Miltonist. In 1967 he wrote a book called "Surprised by Sin", which argued that "Paradise Lost" tricks its readers into sympathising with wickedness in order to educate them in goodness. This had a big influence on how Milton was read. Since then he has written with great acclaim on literary theory, psychoanalysis and legal theory.

How Milton Works
By Stanley Fish

Harvard University Press; 616 pages; $35 and £23.95

Buy it at
Amazon.com
Amazon.co.uk

This new book is billed by its publishers as "the definitive statement on Milton for our time". It is not that. The bulk of it consists of Mr Fish's collected essays on Milton, some of which were written as long ago as 1969. Many contain powerful sections of local analysis of Milton's verse. These are augmented by four new chapters (out of a total of 15).

A cynic might suppose that his publishers are attempting to make a great new event out of a batch of rather elderly material, and a cynic would probably be right. Inevitably, the critical idiom which Mr Fish uses has changed over this 30-year period, although he claims, a little too proudly perhaps, that his central beliefs about Milton have not. The main thesis of this book is that Milton is similarly changeless, and that one set of notions runs through all of his works, from lyrics composed in the 1630s to his epic poetry of the 1660s. The set of notions looks roughly like this. For Milton, all value and all good action depend on obedience to the will of God. Those who seek to obey the will of God see the world in an entirely different way from those who do not. This means that there can be no effective dialogue between those who see the world under the aspect of faith and those who do not. As Mr Fish puts it, "what you believe is what you see is what you are is what you do".

This position is not in itself interesting, nor could you imagine it producing great poetry. And so it is at this point that Mr Fish brings hermeneutics—the craft of interpretation—to his aid. Because divine purpose is inscrutable, it necessarily escapes representation and is only sporadically available even to the intuitions of the faithful. What Milton's readers learn is to treat words as approximate signs of the ineffable. What Milton's protagonists learn is that each moment, even if it appears to be morally neutral, is a moment which tests their ability to interpret and obey the will of God.

Mr Fish's enemies are what he scornfully calls "liberals", who think that Milton's loyalties were divided, that he believed there to be more than one source of value, and that in "Paradise Lost" he was of the devil's party without knowing it. Mr Fish presents instead a Milton who is a no-nonsense zealot. In the process he turns one of the most complex, the most soaringly thoughtful, of English poets into a creature caught in a belief system so simple as to shame a TV evangelist.

Mr Fish insists repeatedly that Milton "is in essence always doing the same thing". Yet Milton lived through the execution of a king (which he defended), the establishment of a commonwealth and the restoration of monarchy (which he attacked, even when it was likely to mean death to do so). His experiences changed how he thought about liberty and about church government, and they changed how he wrote.

Milton also manifestly does acknowledge that there are other sources of value than obedience to an all-knowing deity. Being human, he recognised that things can be valued because they look good to eat and that people can be valued because you love them or admire them. He also valued reason. And it is because he understood that people live each day within a variety of value systems that he could write a great poem about how two people could allow appetite, seemingly rational argument and love to lead them to disobey a divine command.

The Milton described by Mr Fish—hard as rock, obsessed by a single, all-encompassing belief that

obedience to God's will is the only value in the universe—is simply not a poet who could have written "Paradise Lost". It is a sure test of false criticism that it sets out precepts which would deny the possibility of the works that it describes. On this criterion "How Milton Works" is a rare, pure example of criticism which is entirely false.

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Rosemary Verey

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Rosemary Verey, an English gardener, died on May 31st, aged 82

Lorrie Graham

SHE was in the luxury goods' market and her offering was English gardens. Rosemary Verey's own garden was in a 17th-century former rectory called Barnsley House in the Cotswolds. The English climate, warm but not too warm, wet but not too wet, was ideal for the sumptuous garden she created there. But for those who did not have the good fortune to live in England, she was prepared to do her best to create something similar in less blessed countries. Many Americans set their hearts on a Verey garden. It had the kind of cachet attached to, say, Harrods (despite the loss of royal patronage) or a Rolls-Royce (though the marque is now owned by Germans), survivors in the slow decline of England's reputation for quality merchandise. How do you make an English lawn? Sow, and mow for 500 years. Real luxury involved time and experience.

Mrs Verey spared her clients too much waiting. She said she envied perfect lawns but they were not her obsession. Her garden designs would begin to take shape in a few seasons. She created a feeling of timelessness by using styles from the past. So there were hedges of traditional roses, herbaceous borders, laburnum arches revealing statues, and formal areas of clipped boxwood. She helped to create three gardens for Prince Charles at his estate, Highgrove, not far from Barnsley House. One was a kitchen garden. Mrs Verey was particularly clever at making vegetable patches that looked far too pretty to crop. The prince said, "She makes gardening seem the easiest and most natural thing in the world."

It was a princely compliment: "naturalness" in the artificial world of gardening is difficult to pull off. Money helped: the Verey look was a rich person's indulgence. But that was not all. There is a bit of magic in gardening. The prince is said to talk to his plants. Mrs Verey said that plants "love to know they are being cared for". All the same, she gave the impression of demanding that her plants behave or be banished from her Eden. You were not surprised to learn that she was the daughter of a colonel. An American visitor said at the end of a conducted tour of Barnsley House, "She is the most refined lady. We all felt humbled in her presence."

The long tradition

Rosemary Verey was in the tradition of gifted women gardeners that stretches back to Bess of Hardwick, who in the 16th century created some of England's greatest estates. They have tended to be comfortably off (Bess was the richest woman in England after Queen Elizabeth), with ample leisure and a determination to shine in a world run by men. Although mere men could be drafted in to slave with the routine work, no true woman gardener surrenders the command of her territory. Vita Sackville-West (1892-1962), who created a splendid garden at Sissinghurst Castle in Kent, wrote, "For the last 40 years of my life I have broken my back, my finger nails, and sometimes my heart, in the practical pursuit of my favourite occupation."

Mrs Verey discovered what was to become her favourite occupation relatively late in life. An early fancy was to be an economist. But she abandoned university to get married and had four children. Gradually, she recalls, she was "becoming aware of the garden and its seasons". She took advice and started with common plants that are easy to grow. The garden today, though not large, less than three acres (1.2 hectares), conceals many unexpected exotics. What is this? It is a plant from Gethsemane on the Mount of Olives. And this? From Monet's garden at Giverny. And that Greek-style temple? Her husband, an architect, had found it abandoned, dismantled it and rebuilt it in their garden.

She wrote 17 books, some of them now classics. Lecture tours followed. Potential clients lined up. What did they want? Something like Barnsley House, they said. The gardener became the businesswoman. In “Making of a Garden” Mrs Verey wrote:

> When I am invited to help with the planning of a garden I like first to walk slowly around the site, taking in where the warmest corners are likely to be, where the wind comes from, the view, the existing trees, the quality of the soil ... Then it is time to go into the house and look from all the windows...I can build up a picture in my mind of the owners’ preferences...I sometimes imagine that this is where I myself will live, so it must be a place that I will enjoy, but all the time I bear in mind that it is my clients’ garden, individually designed for them, to suit their needs and their way of life.

Not everyone admired the Verey style. Even in the calming world of gardening there is what might be called landscape politics. Minimalist gardens are seen by their practitioners as reflecting modern architecture and painting. They see the simplicity of Stonehenge as a more interesting English tradition than rose hedges. Warming to their theme, they claim that minimalism is right for a world of dwindling resources. You can symbolise the universe in a few square metres.

But “every garden”, said Rosemary Verey, “should have a space where you can walk and sit and feel alone with nature...a quiet and shady place, with mown paths winding between ornamental trees and shrubs, and flowers studding the grass.” Well, if you put it like that...

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Overview

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Economic activity in **America** was slow or decelerating in April and May, according to the Federal Reserve's latest anecdotal survey of economic conditions across the country. The "beige book" also reported that retail sales were sluggish. This finding was backed up by figures showing that the value of retail sales had risen by only 0.1% in May. The Fed survey reported only moderate wage and price increases, with the exception of health-care and energy costs.

There was more bad news from **Japan**, as the economy weakened more than expected in the first quarter. GDP fell at an annual rate of 0.8%, even though the economy was bolstered by a surge in public spending.

The spectre of stagflation threatens to reappear in the **euro area**. Inflationary pressures mounted despite a backdrop of economic slowdown, with GDP growing at an annual rate of just 2% in the first quarter of 2001. In France, consumer prices jumped in May by 0.7% because of rising food prices and resurgent oil prices, lifting the annual rate by half a percentage point. In Germany, consumer-price inflation is 3.5%. This suggests that inflation across the euro area could rise to more than 3% when the next figures are released on June 18th. In the year to April, it ran at 2.9%, well above the 2% target ceiling set by the European Central Bank.

In **Britain**, worries about inflation also returned as consumer-price inflation jumped from 1.8% to 2.1% in the year to May. The underlying rate, which excludes mortgage interest payments, increased from 2.0% to 2.4%, the highest for two years. This unexpected increase prompted a sharp re-evaluation of interest-rate forecasts. The futures markets priced in a rise in the Bank's repo rate from 5.25% to 5.5% by the end of the year. Earnings growth also picked up, rising by 5.2% in the year to April. In another signal that the labour market continues to tighten, the ILO unemployment rate fell to 5.0%, the lowest since this series started in 1984.

Commodities

Wheat prices in the Chicago market edged up, after the Department of Agriculture forecast that America's winter crop would yield only 36m tonnes, a drop of 15% on last year and the smallest for 23 years. It also cut its forecast of China's wheat output this year to 96m tonnes, the lowest for a decade. China's wheat imports are now expected to increase fourfold to 2m tonnes in the year to June 2002.

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Output, demand and jobs

Jun 14th 2001
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% change at annual rate

	GDP		The Economist poll GDP forecasts		Industrial production	Retail sales (volume)	Unemployment % rate	
	1 qtr	1 year	2001	2002	1 year	1 year	latest	year ago
Australia	+ 4.3	+ 2.1 Q1	+ 2.1	+ 3.9	+ 3.1 Q4*	+ 3.0 Q1	6.9 May	6.5
Austria	+ 1.7	+ 2.6 Q4	+ 2.1	+ 2.4	– 5.0 Mar*	– 1.1 Feb	3.7 Apr	3.7
Belgium	+ 1.8	+ 2.4 Q1	+ 2.5	+ 2.6	+ 5.7 Mar*	+ 5.2 Mar	10.0 May*	10.1
Britain	+ 1.7	+ 2.6 Q1	+ 2.2	+ 2.7	– 0.8 Apr	+ 5.9 Apr	5.0 Apr‡	5.7
Canada	+ 2.5	+ 2.6 Q1†	+ 2.2	+ 3.1	+ 0.7 Mar	+ 3.0 Mar	7.0 May	6.6
Denmark	+ 4.9	+ 1.1 Q4	+ 1.8	+ 2.2	+ 1.7 Apr	+ 0.2 Apr	5.4 Apr	5.3
France	+ 2.0	+ 2.7 Q1	+ 2.4	+ 2.5	+ 1.9 Mar	– 0.3 Apr	8.7 Apr	9.9
Germany	+ 1.5	+ 1.6 Q1	+ 1.6	+ 2.3	+ 1.0 Apr	– 0.7 Apr	9.3 May	9.6
Italy	+ 2.8	+ 2.3 Q1	+ 2.1	+ 2.3	– 0.3 Mar	– 0.2 Mar	9.9 Jan	11.2
Japan	– 0.8	– 0.1 Q1	+ 0.5	+ 1.3	– 4.2 Apr	+ 2.1 Mar	4.8 Apr	4.8
Netherlands	+ 0.2	+ 2.0 Q1	+ 2.6	+ 2.9	+ 0.2 Apr	– 3.1 Feb	2.0 Apr§	2.7
Spain	+ 2.9	+ 3.7 Q4	+ 2.8	+ 3.0	+ 0.2 Apr	na	13.1 Apr	14.4
Sweden	+ 2.4	+ 2.6 Q4	+ 2.4	+ 2.9	+ 6.2 Mar	+ 2.3 Apr	3.7 Apr*	4.7
Switzerland	+ 7.4	+ 2.5 Q1	+ 1.9	+ 2.1	+ 5.0 Q4*	+ 2.2 Mar	1.7 May*	1.9
United States	+ 1.3	+ 2.5 Q1	+ 1.6	+ 2.9	– 1.0 Apr	+ 2.5 Apr	4.4 May	4.1
Euro area	+ 2.0	+ 2.5 Q1	+ 2.2	+ 2.5	+ 3.0 Mar	+ 1.6 Mar	8.3 Apr	9.0
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*							
Finland	+ 3.0	+ 5.5 Q4	na	na	+ 0.7 Apr	+ 5.5 Feb	10.3 Apr*	11.0
Greece	na	+ 2.5 2000	na	na	+ 1.9 Dec	+11.8 Jan	na	na
Iceland	na	+ 3.6 2000	na	na	+ 4.2 1999	na	1.5 Apr	1.5
Ireland	na	+11.0 Q3	na	na	+17.0 Apr*	+ 1.6 Mar	3.6 Apr	4.3
Luxembourg	na	+ 8.5 2000	na	na	+ 0.2 Feb*	+ 9.4 Nov	2.5 Apr	2.6
New Zealand	+ 2.2	+ 1.6 Q4	na	na	+ 0.9 Q4*	+ 1.7 Q1	5.4 Q1	6.4
Norway	+ 0.9	+ 0.3 Q1	na	na	+ 1.1 Apr	– 1.0 Apr	3.7 Q1	3.9
Portugal	+ 2.2	+ 3.4 Q4	na	na	+ 4.5 Apr*	– 0.6 Feb	3.8 Q4	4.1

*Not seasonally adjusted. †New series. ‡Feb-Apr; claimant count rate 3.2% in May. §Feb-Apr.

Text refers only to the first 16 countries listed

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Prices and wages

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From The Economist print edition

% change at annual rate

	Consumer prices*			The Economist poll consumer prices forecast		Producer prices*			Wages/earnings		
	1 year		year ago	2001	2002	1 year		year ago	1 year		year ago
Australia	+ 6.0	Q1	+ 2.8	+ 3.6	+ 2.3	+ 5.2	Q1	+ 5.6	+ 5.6	Q1	+ 2.9
Austria	+ 2.9	Apr	+ 1.9	+ 1.9	+ 1.4	+ 3.1	May	+ 2.7	+ 2.6	Apr	+ 2.0
Belgium	+ 3.1	May	+ 2.2	+ 2.1	+ 1.8	+ 3.8	Mar	+ 8.6	+ 1.9	Q1	+ 3.3
Britain	+ 2.1	May	+ 3.1	+ 2.0	+ 2.3	+ 0.6	May	+ 2.5	+ 5.2	Apr	+ 5.1
Canada	+ 3.6	Apr	+ 2.1	+ 2.4	+ 2.1	+ 2.7	Apr	+ 5.7	+ 1.3	Mar	+ 3.0
Denmark	+ 2.7	May	+ 3.3	+ 2.3	+ 2.2	+ 3.6	Apr	+ 5.7	+ 3.8	Q4	+ 4.1
France	+ 2.3	May	+ 1.5	+ 1.5	+ 1.5	+ 2.9	Apr	+ 3.5	+ 5.0	Q4	+ 3.4
Germany	+ 3.5	May	+ 1.4	+ 2.3	+ 1.5	+ 4.1	Apr	+ 4.4	+ 1.7	Mar*	+ 2.1
Italy	+ 3.0	May	+ 2.5	+ 2.5	+ 1.9	+ 4.3	Apr	+ 5.4	+ 2.6	Apr*	+ 2.1
Japan	− 0.4	Apr	− 0.8	− 0.4	− 0.3	+ 0.9	May	− 0.6	+ 0.2	Apr	+ 2.2
Netherlands	+ 4.9	May	+ 2.4	+ 4.0	+ 2.3	+ 5.6	Apr	+ 7.3	+ 3.3	Apr	+ 3.4
Spain	+ 4.2	May	+ 3.2	+ 3.3	+ 2.6	+ 2.8	Apr	+ 5.7	+ 2.2	Q4	+ 2.4
Sweden	+ 2.8	Apr	+ 1.1	+ 1.9	+ 1.7	+ 3.3	Apr	+ 3.3	+ 2.1	Mar*	+ 3.4
Switzerland	+ 1.8	May	+ 1.6	+ 1.2	+ 1.2	+ 0.9	Apr	+ 2.8	+ 0.2	1999	+ 0.7
United States	+ 3.3	Apr	+ 3.1	+ 2.9	+ 2.4	+ 3.7	Apr	+ 3.6	+ 4.3	May	+ 3.6
Euro area	+ 2.9	Apr	+ 1.9	+ 2.3	+ 1.7	+ 4.1	Apr	+ 4.7	+ 2.4	Q4	+ 2.3
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*										
Finland	+ 3.4	May	+ 2.7	na	na	+ 3.0	Apr	+ 7.1	+ 5.0	Q1*	+ 3.5
Greece	+ 3.6	May	+ 2.9	na	na	+ 4.3	Mar	+ 7.9	na		na
Iceland	+ 5.5	May	+ 5.9	na	na	+ 5.7	May	+ 3.6	+ 9.2	Apr	+ 5.3
Ireland	+ 5.4	May	+ 5.2	na	na	+ 2.9	Apr	+ 5.4	+ 7.4	Q3*	+ 6.6
Luxembourg	+ 3.3	May	+ 2.5	na	na	+ 3.6	Mar	+ 3.2	+ 8.4	Oct*	+ 1.7
New Zealand	+ 3.1	Q1	+ 1.5	na	na	+ 7.8	Q1	+ 4.9	+ 1.8	Q1	+ 1.4
Norway	+ 4.3	May	+ 2.8	na	na	+ 4.6	May	+ 8.0	+ 4.3	Q4*	+ 4.0
Portugal	+ 4.5	Apr	+ 2.1	na	na	+ 3.2	Apr	+17.7	+ 2.2	Feb*	+ 2.8

*Not seasonally adjusted.

Text refers only to the first 16 countries listed

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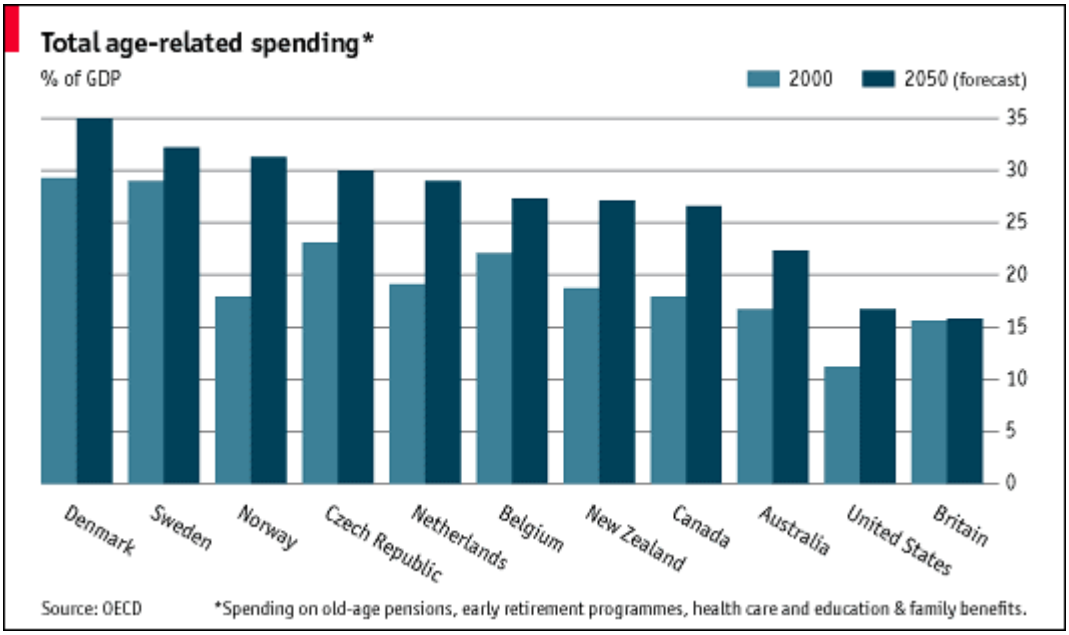
Total age-related spending

Jun 14th 2001
From The Economist print edition

New estimates from the OECD show that the age structure of the population affects as much as 40-60% of public spending in developed countries. Age-related expenditure will increase markedly over the next 50 years, as an older population demands extra spending on public pensions and health care. Any offset from lower public spending on children thanks to low birth rates will only be modest.



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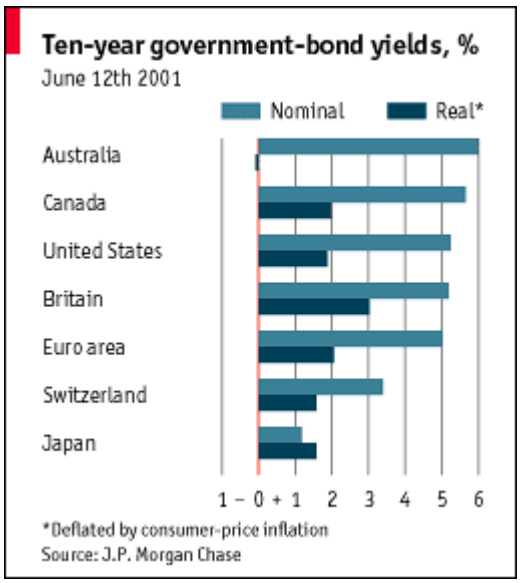
Ten-year government-bond yields

Jun 14th 2001
From The Economist print edition

Real bond yields diverge markedly from nominal yields. Of those in the chart, Australia's yield the most in nominal terms. But if inflation is taken into account, British bonds yield the most.



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Commodity price index

Jun 14th 2001
From The Economist print edition

1995=100

	Jun 5th	Jun 12th*	% change on one month	% change on one year
Dollar index				
All items	70.2	69.7	– 2.5	– 5.0
Food	67.4	67.8	– 1.2	– 6.3
Industrials				
All	74.0	72.3	– 4.1	– 3.5
Nfa†	73.2	71.6	– 4.3	– 0.8
Metals	74.6	72.9	– 3.9	– 5.6
Sterling index				
All items	78.5	79.7	+ 0.5	+ 4.2
Euro index				
All items	108.9	108.0	+ 0.9	+ 7.4
Yen index				
All items	89.8	90.4	– 3.7	+ 8.4
Gold				
$ per oz	265.75	269.60	+ 0.8	– 7.1
West Texas Intermediate				
$ per barrel	27.77	29.52	+ 2.4	– 9.5

* Provisional. † Non-food agriculturals.

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Stockmarkets

Jun 14th 2001
From The Economist print edition

Market indices

	Jun 13th	2001 high	2001 low	% change on one week	% change on record high	% change on Dec 31st 2000 in local currency	% change on Dec 31st 2000 in $ terms
Australia (All Ordinaries)	3,324.5	3,370.7	3,094.3	- 0.9	- 1.4	+ 5.4	+ 0.2
Austria (ATX)	1,244.9	1,244.9	1,052.2	+ 0.7	-28.3	+16.0	+ 5.2
Belgium (Bel 20)	2,857.1	3,030.4	2,591.6	- 1.4	-22.4	- 5.5	-14.3
Britain (FTSE 100)	5,820.2	6,334.5	5,314.8	- 1.4	-16.0	- 6.5	-13.1
Canada (Toronto Composite)	8,012.7	9,348.4	7,415.5	- 2.2	-29.6	-10.3	-11.2
Denmark (Copenhagen SE)	908.5	1,002.1	818.3	- 1.5	-12.6	+ 0.2	- 9.0
France (SBF 250)	3,438.3	3,820.2	3,107.9	- 2.7	-21.7	- 8.8	-17.3
(CAC 40)	5,353.6	5,998.5	4,824.8	- 2.6	-22.7	- 9.7	-18.1
Germany (Xetra DAX)	6,111.9	6,795.1	5,388.0	- 1.3	-24.2	- 5.0	-13.8
Italy (BCI)	1,696.6	1,948.4	1,609.6	nil	-22.3	-11.5	-19.7
Japan (Nikkei 225)	12,823.5	14,529.4	11,819.7	- 2.7	-67.0	- 7.0	-12.7
(Topix)	1,272.7	1,441.0	1,162.0	- 2.7	-55.9	- 0.9	- 7.0
Netherlands (AEX)	576.7	642.3	518.3	- 2.2	-17.8	- 9.5	-18.0
Spain (Madrid SE)	913.5	963.9	818.6	- 0.3	-20.3	+ 3.7	- 5.9
Sweden (Affarsvarlden Gen)	240.1	292.7	217.2	- 5.2	-39.9	-13.4	-24.6
Switzerland (Swiss Market)	7,475.8	8,135.4	6,574.0	- 1.4	-11.1	- 8.1	-17.0
United States (DJIA)	10,871.6	11,337.9	9,389.5	- 1.8	- 7.3	+ 0.8	+ 0.8
(S&P 500)	1,241.6	1,373.7	1,103.3	- 2.2	-18.7	- 6.0	- 6.0
(Nasdaq Comp)	2,121.7	2,859.2	1,638.8	- 4.3	-58.0	-14.1	-14.1
Europe (FTSE Eurotop 300) *	1,423.2	1,545.5	1,279.0	- 2.4	-16.5	- 7.2	-15.8
Euro area (FTSE Ebloc 100) *	1,271.8	1,404.1	1,143.9	- 2.7	-18.0	- 8.6	-17.2
World (MSCI) †	1,103.4	1,249.2	1,014.6	- 2.2	-23.8	na	- 9.6
World bond market (Salomon) ‡	427.4	447.8	426.2	- 0.1	- 7.1	na	- 3.8

*In euro terms. † Morgan Stanley Capital International index includes individual markets listed above plus eight others, in dollar terms.
‡ Salomon Smith Barney World Government Bond Index, total return, in dollar terms.

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Trade, exchange rates and budgets

Jun 14th 2001
From The Economist print edition

	Trade balance*, $bn latest 12 months		Current account $bn latest 12 mths		The Economist poll % of GDP, forecast 2001	2002	Exchange rate trade-weighted† Jun 13th	year ago	Currency units per $ Jun 13th	year ago	per £	per euro	per ¥100	Budget balance % of GDP 2001‡
Australia	− 2.6	Apr	− 12.9	Q1	− 2.4	− 2.5	74.7	77.8	1.89	1.66	2.63	1.61	1.56	0.1
Austria	− 5.1	Feb	− 4.2	Mar	− 2.5	− 2.4	99.8	100.3	16.2	14.3	22.4	13.8	13.3	-0.6
Belgium	+ 12.8	Mar	+ 11.6	Dec	+ 4.1	+ 4.3	98.2	99.3	47.4	42.0	65.8	40.3	38.9	0.7
Britain	− 44.3	Mar	− 24.5	Q4	− 2.0	− 2.1	105.8	103.4	0.72	0.67	–	0.61	0.59	1.2
Canada	+ 40.4	Mar	+ 22.2	Q1	+ 1.5	+ 1.1	79.6	80.4	1.52	1.47	2.11	1.29	1.25	2.6
Denmark	+ 5.9	Mar	+ 3.7	Mar	+ 1.4	+ 1.5	101.2	101.0	8.76	7.78	12.2	7.46	7.19	2.9
France	+ 0.9	Mar	+ 23.5	Mar	+ 1.8	+ 1.8	100.7	102.2	7.70	6.84	10.7	6.56	6.33	-0.5
Germany	+ 54.4	Apr	− 21.3	Apr	− 1.2	− 0.9	97.5	98.9	2.30	2.04	3.19	1.96	1.89	-1.7
Italy	+ 1.6	Mar	− 5.6	Feb	− 0.3	nil	71.9	72.9	2,274	2,018	3,156	1,936	1,868	-1.3
Japan	+ 98.9	Apr	+106.4	Apr	+ 2.2	+ 2.2	141.1	153.1	122	107	169	104	–	-6.3
Netherlands	+ 16.5	Mar	+ 16.0	Q1	+ 3.7	+ 3.8	97.0	98.2	2.59	2.30	3.59	2.20	2.13	1.3
Spain	− 39.1	Mar	− 17.3	Feb	− 2.9	− 2.6	73.6	74.5	195	173	271	166	161	nil
Sweden	+ 11.0	Mar	+ 5.5	Apr	+ 2.2	+ 2.2	74.9	86.1	10.83	8.54	15.0	9.22	8.90	3.6
Switzerland	− 0.4	Apr	+ 31.1	Q4	+11.8	+11.4	106.9	105.6	1.79	1.63	2.49	1.53	1.47	na
United States	−454.6	Mar	−434.9	Q4	− 4.2	− 4.0	120.4	108.9	–	–	1.39	0.85	0.82	2.1
Euro area	− 4.5	Mar	− 32.6	Mar	− 0.3	− 0.2	76.7	80.7	1.17	1.04	1.63	–	0.97	-0.6
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*													
Finland	+ 13.7	Apr	+ 9.7	Mar	na	na	77.4	77.3	6.73	6.20	9.34	5.73	5.53	5.3
Greece	− 7.5	Q4	− 7.7	Jan	na	na	57.0	58.3	385	351	534	328	316	nil
Iceland	− 0.4	Apr	− 0.9	Q4	na	na	na	na	97.1	75.8	135	82.6	79.7	2.4
Ireland	+ 27.6	Mar	− 0.7	Q4	na	na	86.1	88.4	1.12	0.82	1.55	0.95	0.92	4.5
Luxembourg	− 2.4	Jan	+ 1.6	Q4	na	na	98.2	99.3	45.6	42.0	63.3	38.8	37.5	3.6
New Zealand	− 0.3	Apr	− 2.7	Q4	na	na	81.0	82.9	2.36	2.10	3.28	2.01	1.94	1.0
Norway	+ 27.5	Apr	+ 24.9	Mar	na	na	95.2	91.9	9.11	8.58	12.6	7.76	7.48	15.3
Portugal	− 12.4	Feb	− 10.1	Mar	na	na	88.8	89.5	227	209	315	193	186	-1.2

*Merchandise. Australia, Britain, France, Canada, Japan and United States imports fob, exports fob. All others cif/fob. †1990=100, Bank of England. ‡OECD estimate.

Text refers only to the first 16 countries listed

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Money and interest rates

Jun 14th 2001
From The Economist print edition

	Money supply* % change on year ago			Interest rates % p.a. (Jun 13th 2001)					
				3-mth money market		2-year	10-year gov't bonds		corporate
	narrow	broad		latest	year ago	gov't bonds	latest	year ago	bonds
Australia	+13.5	+ 7.0	Apr	5.01	6.20	5.24	5.86	6.16	7.25
Britain	+ 7.7	+ 7.9	Apr	5.22	6.11	5.44	5.20	5.12	6.80
Canada	+11.4	+ 4.8	Apr	4.27	5.60	4.76	5.68	5.87	7.17
Denmark	+ 1.5	– 3.5	Apr	5.05	5.05	4.86	5.32	5.57	7.18
Japan	+ 7.0	+ 2.9	May	0.01	0.03	0.03	1.16	1.67	1.35‡
Sweden	+ 5.8	– 0.3	Apr	4.03	3.96	4.71	5.38	4.96	5.63
Switzerland	– 2.2	+ 2.4	Apr	3.11	3.39	3.05	3.39	3.94	4.03
United States	+ 0.1	+10.2	Apr	3.79	6.57	4.04	5.26	6.04	7.03
Euro area†	+ 1.8	+ 5.2	Apr	4.47	4.69	4.37	5.02	5.08	5.67

*Narrow: M1 except Britain and Sweden M0, broad: M2 or M3 except Britain M4. †Germany for bonds. ‡ New series. Benchmarks: US 30-year 5.66%, Japan No.231 1.81%. Central bank rates: US fed funds 4.00%, ECB refinancing 4.50%, BOJ overnight call 0.01%, BOE repo 5.25%. Sources: Commerzbank, Danske Bank, J.P. Morgan Chase, Royal Bank of Canada, OM Fixed Income Exchange, Warburg Dillon Read, DRI-WEFA, Westpac, Thomson Financial Datastream. Rates cannot be construed as banks' offers.

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Overview

Jun 14th 2001
From The Economist print edition

Some of the largest East Asian economies are still running big trade surpluses. In the 12 months to May, China's surplus was $21.1 billion, South Korea's $15 billion and Taiwan's $11.4 billion.

Stockmarkets in South-East Asia rose strongly. Kuala Lumpur rose by 6.1% on optimism about prospects for Malaysia. Manila rose by 5.3% as low valuations attracted bargain-hunters. Jakarta rose by 4.9%, boosted by rumours of a cabinet reshuffle that would bolster political confidence.

However, markets fell in some other emerging markets. Warsaw dropped by 4.6% on investor worries about privatisation plans.

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Financial markets

Jun 14th 2001
From The Economist print edition

	Currency units			Interest rates	Stockmarkets	% change on		
	per $		per £	short-term	Jun 13th		Dec 31st 2000	
	Jun 13th	year ago	Jun 13th	% p.a.		one week	in local currency	in $ terms
China	8.28	8.28	11.5	na	2,337.9	+0.4	+6.6	+6.6
Hong Kong	7.80	7.79	10.8	3.84	13,523.3	-0.4	-10.4	-10.4
India	47.0	44.7	65.3	7.37	3,501.6	+1.3	-11.8	-12.5
Indonesia	11,225	8,520	15,578	16.67	417.1	+4.9	+0.2	-13.7
Malaysia	3.80	3.80	5.27	3.30	598.7	+6.1	-11.9	-11.9
Philippines	51.4	42.4	71.3	11.06	1,462.7	+5.3	-2.1	-4.7
Singapore	1.82	1.72	2.52	2.25	1,696.0	+1.0	-12.0	-16.0
South Korea	1,292	1,114	1,793	5.67	614.1	+2.7	+21.7	+19.1
Taiwan	34.4	30.7	47.7	4.10	5,209.7	-0.2	+9.8	+5.7
Thailand	45.4	39.0	62.9	3.50	324.9	+4.7	+20.7	+15.5
Argentina	1.00	1.00	1.39	9.38	446.0	+1.6	+7.0	+6.8
Brazil	2.41	1.81	3.35	16.81	15,462.6	+0.9	-0.9	-19.8
Chile	614	531	852	3.45**	5,456.5	+0.4	+12.1	+4.8
Colombia	2,307	2,114	3,201	12.72	873.9	+0.2	+22.6	+18.9
Mexico	9.12	9.79	12.6	9.51	6,802.4	+0.2	+20.3	+26.9
Peru	3.52	3.48	4.9	11.17	1,380.0	-2.0	+14.2	+14.5
Venezuela	716	681	994	11.00	7,462.7	-3.3	+9.8	+7.3
Egypt	3.88	3.46	5.38	9.08	6,285.9	+0.8	-18.0	-17.7
Israel	4.15	4.10	5.76	5.09	410.5	-1.6	-17.0	-19.2
South Africa	8.09	6.96	11.2	10.70	9,263.6	-0.7	+11.3	+4.0
Turkey	1,243,000	613,125	1,725,035	59.00	11,284.4	-3.8	+19.6	-35.5
Czech Republic	39.8	37.6	55.2	5.10	433.8	+1.7	-9.3	-14.3
Hungary	290	271	402	11.14	6,755.8	-3.4	-13.9	-16.2
Poland	3.96	4.41	5.49	17.48	14,545.1	-4.6	-18.5	-14.9
Russia	29.1	28.4	40.4	25.00	210.1†	-1.5	+49.1	+46.7
EMF (MSCI)‡	1.00	1.00	1.39	na	331.0	+0.5	na	-0.8
EMBI+§	1.00	1.00	1.39	na	217.8	+1.3	na	+7.9

*Last week's rate. **Inflation adjusted. †In dollar terms. ‡Emerging Markets Free. §J.P. Morgan Chase's Emerging Markets Bond Index Plus.

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Economy

Jun 14th 2001
From The Economist print edition

	% change on year earlier						Latest 12 months, $bn				Foreign reserves* $bn, latest	
	GDP		Industrial production		Consumer prices		Trade balance		Current account			
China	+ 8.1	Q1	+10.2	May	+ 1.7	May	+21.1	May	+20.5	2000	178.0	Feb
Hong Kong	+ 2.5	Q1	− 0.2	Q4	− 1.4	Apr	−11.9	Apr	+ 8.8	Q4	114.7	May
India	+ 5.7	Q3	+ 1.3	Mar	+ 2.3	Apr	− 5.7	Apr	− 5.4	Q4	39.9	Apr
Indonesia	+ 4.0	Q1	+ 4.5	Q4	+10.8	May	+26.1	Apr	+ 5.5	Q3	22.1	Apr
Malaysia	+ 3.2	Q1	− 0.3	Apr	+ 1.6	Apr	+15.6	Apr	+ 8.4	Q4	26.8	Mar
Philippines	+ 2.5	Q1	− 2.0	Mar	+ 6.5	May	+ 7.3	Mar	+ 9.5	Feb	12.8	Mar
Singapore	+ 4.5	Q1	− 0.8	Apr	+ 2.0	Apr	+ 4.2	Apr	+21.8	Q1	77.6	Mar
South Korea	+ 3.7	Q1	+ 5.7	Apr	+ 5.4	May	+15.0	May	+14.0	Apr	93.4	May
Taiwan	+ 1.1	Q1	− 5.9	Apr	− 0.2	May	+11.4	May	+12.0	Q1	110.6	Mar
Thailand	+ 3.1	Q4	+ 0.7	Apr	+ 2.8	May	+ 3.1	Apr	+ 6.9	Apr	31.5	Apr
Argentina	− 2.6	Q4	+ 8.6	Apr	+ 0.2	May	+ 1.6	Apr	− 9.4	Q4	20.5	Apr
Brazil	+ 3.8	Q1	+ 6.1	Apr	+ 7.1	Apr	+34.7	Apr	−26.6	Apr	34.1	Mar
Chile	+ 3.3	Q1	+ 3.1	Apr	+ 3.7	May	+ 1.5	Apr	− 1.4	Q1	14.3	Apr
Colombia	+ 1.8	Q1	+ 4.0	Apr	+ 7.9	May	+ 0.6	Mar	− 0.1	Q4	9.7	Apr
Mexico	+ 1.9	Q1	− 3.1	Apr	+ 7.0	May	− 9.5	Apr	−17.8	Q1	40.3	Apr
Peru	− 0.9	Apr	− 6.3	Mar	+ 2.6	May	− 0.4	Mar	− 1.7	Q4	8.2	Mar
Venezuela	+ 3.5	Q1	na		+12.6	May	+17.5	Nov	+12.5	Q1	11.5	Apr
Egypt	+ 6.5	2000†	+ 9.4	2000†	+ 2.4	Mar	−10.4	Q4	− 0.8	Q4	12.9	Feb
Israel	+ 1.8	Q1	− 1.0	Mar	+ 1.2	Apr	− 7.5	May	− 0.7	Q3	23.5	Apr
South Africa	+ 2.7	Q1	+ 7.3	Apr	+ 6.5	Apr	+ 3.7	Apr	− 0.5	Q4	6.2	Mar
Turkey	+ 8.3	Q4	−10.5	Apr	+52.4	May	−26.3	Mar	− 8.1	Mar	18.5	Apr
Czech Republic	+ 3.9	Q4	+11.4	Apr	+ 5.0	May	− 3.6	Apr	− 2.7	Q1	13.0	Apr
Hungary	+ 4.4	Q1	+ 9.7	Apr	+10.8	May	− 2.4	Apr	− 1.7	Apr	11.3	Apr
Poland	+ 2.4	Q4	+ 3.6	Apr	+ 6.6	Apr	−10.0	Apr	− 8.8	Apr	27.1	Mar
Russia	+ 6.8	Q4	+ 5.2	Apr	+25.0	May	+60.7	Mar	+45.9	Q1	25.9	Mar
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*											
Pakistan	+ 5.6	2000†	+ 7.9	Oct	+ 4.2	Mar	− 1.7	Apr	− 2.5	1999	1.2	Apr
Saudi Arabia	− 0.8	1999	na		− 0.2	Mar	+24.9	1999	+ 0.4	1999	16.9	Mar

*Excluding gold, except Singapore; IMF definition. †Year ending June.

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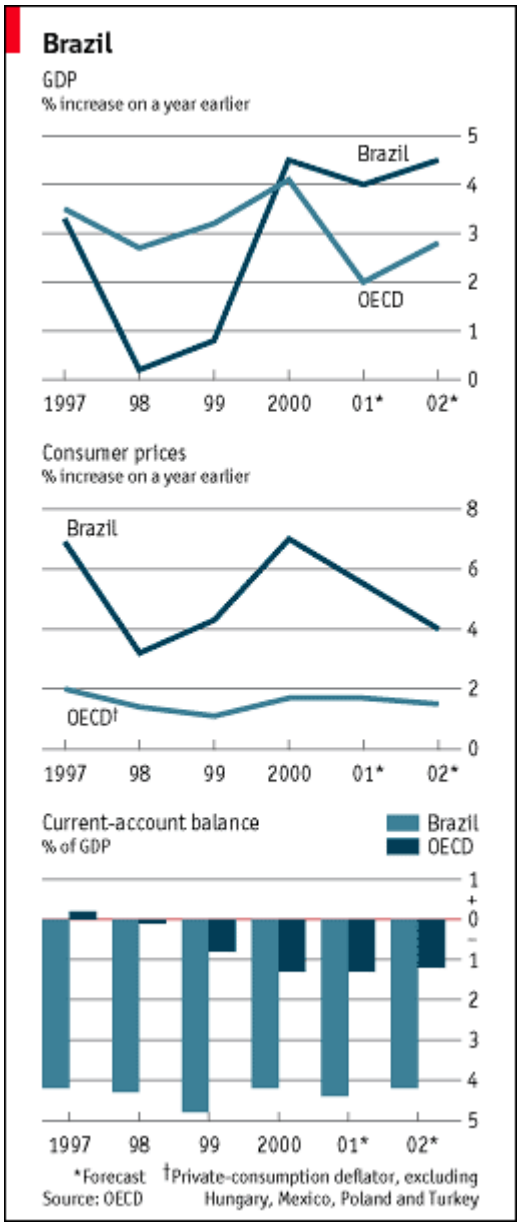
Brazil

Jun 14th 2001
From The Economist print edition

Economic reforms have enhanced Brazil's growth prospects, argues the OECD in its first survey of the country. But a big current-account deficit means that the economy is vulnerable to external shocks. The OECD calls for more tax and public-pension reforms. It also recommends that the central bank be made independent to keep inflation in check.



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